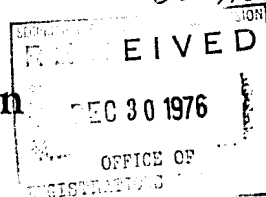


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PROSPECTUS

G034000
GAF Corporation
650,000 Shares
Common Stock
(Par Value \$1 Per Share)



JAN 10 1977

Plan for the Sale of Restricted and Unrestricted Common Stock to Employees Who Perform Executive, Administrative or Supervisory Functions (the "Stock Purchase Plan").

THESE SECURITIES HAVE NOT BEEN APPROVED OR DISAPPROVED BY THE
SECURITIES AND EXCHANGE COMMISSION NOR HAS THE COMMISSION
PASSED UPON THE ACCURACY OR ADEQUACY OF THIS PROSPECTUS.
ANY REPRESENTATION TO THE CONTRARY IS A CRIMINAL OFFENSE.

GAF Corporation (the "Company") is offering by this Prospectus a maximum of 650,000 shares of its Common Stock to those key employees of the Company and its subsidiaries who may from time to time be designated as eligible to purchase shares pursuant to the Stock Purchase Plan of the Company described in this Prospectus. This offer is made at the price and on the terms and conditions contained in a letter agreement which will be entered into by the Company and the offeree at the time an offer is made. The Common Stock of the Company is listed on the New York Stock Exchange. The price of shares issued as "Restricted Shares" must be at least 50%, and the price of shares issued as "Unrestricted Shares" must be at least 80%, of the closing price of the Company's Common Stock on the New York Stock Exchange on the last trading day on which such stock was traded preceding the date on which an employee is designated as one to whom such shares may be offered for sale. See "Description of Stock Purchase Plan."

The last reported sale price of the Common Stock on the Consolidated Tape Network A on November 30, 1976 was \$12.125 per share.

This Prospectus is also applicable to any resale or offer of shares covered by the Plan by any purchaser or his transferee if it might be deemed, the Company not so conceding, that such purchaser or transferee may be an underwriter, as defined in the Securities Act of 1933, with respect to such shares and if he might effectuate any sale of such shares in circumstances requiring the delivery of a prospectus. Any broker or dealer participating in any such distribution may be deemed to be an underwriter within the meaning of such Act.

If any of the shares covered by the Plan are reacquired by the Company from purchasers pursuant to the Plan, this Prospectus is also applicable to any offer or sale of such shares to the public by the Company on the New York Stock Exchange at then current market prices.

The shares to which this Prospectus relates have been approved for listing on the New York Stock Exchange, subject to official notice of issuance to the extent not already issued.

No person has been authorized by the Company to give any information or to make any representations not contained in this Prospectus, and, if given or made, such information or representations must not be relied upon as having been so authorized. This Prospectus does not constitute an offer of Common Stock in any State or other jurisdiction to any person to whom it is unlawful to make such offer in such State or other jurisdiction.

The date of this Prospectus is December 29, 1976.

The Company has filed with the Securities and Exchange Commission, Washington, D.C. 20549 a Registration Statement under the Securities Act of 1933 covering the shares of Common Stock to which this Prospectus relates. This Prospectus does not contain all the information set forth in the Registration Statement, certain portions of which have been omitted pursuant to the rules and regulations of the Securities and Exchange Commission. The information so omitted may be obtained in the Commission's principal office at 500 North Capitol Street, N.W., Washington, D.C. upon payment of the fees prescribed by the Commission.

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The Company is subject to the informational requirements of the Securities Exchange Act of 1934 and in accordance therewith files reports and other information with the Securities and Exchange Commission. Information concerning its directors and officers, their remuneration and options granted to them, its principal holders of securities, and any material interests of any such persons in transactions with it, as of particular dates, is set forth in proxy statements distributed to its stockholders and filed with the Commission. Such reports, proxy statements and other information can be inspected at the Commission's principal office in Washington, D.C., and copies of such material can be obtained from the Commission at prescribed rates. The Company's Common Stock is listed on the New York Stock Exchange, and reports, proxy material and other information concerning the Company also can be inspected at the library of the Exchange, 20 Broad Street, New York, New York 10005.

Except where otherwise indicated, this Prospectus speaks as of its date of issue. Statements contained in this Prospectus as to the contents of any document referred to are not necessarily complete, and in each instance reference is made to the copy of the document filed as an exhibit to the Registration Statement, each such statement being qualified in all respects by this reference.

GENERAL

The Company was incorporated in Delaware in 1929 as American I.G. Chemical Corporation and changed its name to General Aniline & Film Corporation in 1939 and to GAF Corporation in 1968. References to the Company, unless the context otherwise requires, include GAF Corporation and its consolidated subsidiaries.

In 1942 over 90% of the Company's then outstanding stock was vested by the Federal Government in the Alien Property Custodian under the Trading with the Enemy Act. After recapitalization of the Company in 1964, the stock owned by the Federal Government was sold in a public offering in March 1965.

Since 1965, the Company has made a number of acquisitions pursuant to which it became engaged in the manufacturing, mining, distributing and selling of various building materials, resilient flooring and industrial products and expanded the scope of its traditional chemical, photographic products and reprographic business systems operations.

The principal executive offices of the Company are located at 140 West 51st Street, New York, New York 10020, telephone number (212) 582-7600.

USE OF PROCEEDS

The net proceeds from the sale by the Company, from time to time, of the shares of Common Stock covered by this Prospectus will be added to the general funds of the Company.

GAF CORPORATION AND CONSOLIDATED SUBSIDIARIES
CONSOLIDATED STATEMENT OF INCOME

The following five-year Consolidated Statement of Income has been examined by Haskins & Sells, independent certified public accountants, whose opinion with respect thereto appears elsewhere in this Prospectus. This statement should be read in conjunction with the other consolidated financial statements and the notes thereto included elsewhere in this Prospectus.

	Year Ended December 31,				
	1975	1974	1973	1972	1971
	(Note B)	(Note B)	(Note B)	(Note B)	(Note B)
	Dollars in Thousands Except Per Share Amounts				
Net Sales (Note E)	\$964,421	\$948,809	\$848,886	\$768,460	\$683,762
Costs and Expenses:					
Costs of products sold (Notes C, D and E)	691,104	672,930	592,999	535,395	477,236
Distribution and selling (Note E)	134,255	129,686	121,741	110,143	98,008
Advertising	18,409	19,378	18,201	16,697	14,208
Research and development (Note I)	15,272	15,011	13,865	13,656	12,177
Administrative and general	45,623	44,216	38,735	34,446	31,192
Interest (Note F)	18,555	16,792	12,068	10,237	10,359
Operating loss of discontinued operations (Note E) ..	—	—	—	—	4,343
Total Costs and Expenses	921,218	898,013	797,809	720,574	647,523
Other Income (Charges):					
Gain on sale of technology and know-how (Note A) ..	4,000	—	—	—	—
Office relocation expenses (Note G)	(859)	(5,045)	(281)	—	—
Gain on reacquisition of 5% convertible notes	—	5,523	6,359	—	—
Phase-out of Linden dyestuff and pigment operations (Note H) ..	—	—	(5,942)	—	—
Other income (charges) — net (Note I)	(35)	(1,721)	4,171	2,463	1,403
Total Other Income (Charges) — Net	3,306	(1,243)	4,327	2,463	1,403
Income Before Income Taxes and Extraordinary Items ..	46,509	49,553	55,604	50,349	37,642
Income Taxes (Notes J, I and S)	15,583	21,036	23,785	22,643	15,735
Income Before Extraordinary Items (Note H)	30,940	28,517	31,819	27,706	21,907
Extraordinary Items (Note E)	—	—	—	—	(8,433)
Net Income	\$ 30,940	\$ 28,517	\$ 31,819	\$ 27,706	\$ 13,474
Earnings Applicable to Common Stock:					
Net income	\$ 30,940	\$ 28,517	\$ 31,819	\$ 27,706	\$ 13,474
Less preferred stock dividend requirements	3,635	3,705	3,726	3,759	3,802
Earnings applicable to common stock	\$ 27,311	\$ 24,812	\$ 28,093	\$ 23,947	\$ 9,672
Primary Earnings per Common Share (Note I):					
Income before extraordinary items	\$2.06	\$1.84	\$2.06	\$1.75	\$1.33
Extraordinary items	—	—	—	—	(.62)
Net income	\$2.06	\$1.84	\$2.06	\$1.75	\$.71
Fully Diluted Earnings per Common Share (Note I):					
Income before extraordinary items	\$1.79	\$1.62	\$1.74	\$1.49	\$1.19
Extraordinary items	—	—	—	—	•
Net income	\$1.79	\$1.62	\$1.74	\$1.49	•
Cash Dividends Declared:					
Per preferred share	\$1.20	\$1.20	\$1.20	\$1.20	\$1.20
Per common share	\$.52	\$.46	\$.42	\$.40	\$.40
Weighted Average Number of Shares of Common Stock Outstanding (in thousands)	13,237	13,518	13,631	13,687	13,609

* Figure omitted because not dilutive.

Numerical note references are to Notes to Consolidated Financial Statements included elsewhere in this Prospectus.

(Notes to Consolidated Statement of Income are on the following pages.)

GAF CORPORATION AND CONSOLIDATED SUBSIDIARIES

NOTES TO CONSOLIDATED STATEMENT OF INCOME

Note A:

During 1975 the Company and Chemische Werke Hüls, A.G. ("Hüls"), a West German company, formed a joint venture (GAF/Hüls Chemie G.m.b.H.) to construct and operate a butanediol manufacturing plant in West Germany. The joint venture is owned equally by the Company and Hüls. The investment is included in Other investments and advances and has been accounted for by the equity method.

In the second quarter of 1975, the Company sold certain technology and know-how to the joint venture resulting in a gain of \$4,000,000 after elimination entries. This gain is not subject to U.S. income tax.

Note B:

The Financial Accounting Standards Board recently issued a Statement on accounting for the translation of foreign currency. The principal provisions of the Statement, as applied to the Company, require that exchange gains or losses be included in net income and that inventories be translated at historical rates. During the fourth quarter of 1975, the Company revised its previous policy (net translation gains were deferred and inventories were translated at current rates) to adopt the provisions of the new Statement. Previously reported financial statements for 1974 and 1973 have been restated accordingly. The effect on years prior to 1973 is not significant.

The effect of the change on net income for 1975 was an increase of \$1,711,000 (\$.13 per share — primary; \$.10 per share — fully diluted). Previously reported net income for 1974 has been reduced by \$3,976,000 (\$.29 per share — primary; \$.22 per share — fully diluted). Previously reported net income for 1973 has been increased by \$2,395,000 (\$.21 per share — primary; \$.16 per share — fully diluted).

After tax foreign exchange gains (losses) are included in income before extraordinary items as follows:

Year	Amount
1975	\$(1,257,000)
1974	(1,612,000)
1973	1,830,000
1972	(447,000)

An after tax gain of \$992,000 was treated as an extraordinary credit in 1971 (Note E).

Note C:

Effective with the year ended December 31, 1974, the Company changed its method of accounting for dyestuffs and pigments inventories from the average cost method to the last-in, first-out (LIFO) method. The change to the LIFO method was made because management believes that the LIFO method more realistically matches current costs with current revenues. The effect of the change was to reduce the inventory at December 31, 1974 by \$3,852,000 and net income for the year then ended by \$1,786,000 (\$.13 per share — primary; \$.10 per share — fully diluted). There is no effect from the change on periods prior to 1974 since the December 31, 1973 inventory as previously reported was the opening inventory under the LIFO method. The current cost for these inventories, determined on an average cost basis, exceeded their LIFO valuation by \$4,712,000 and \$3,852,000 at December 31, 1975 and 1974, respectively.

GAF CORPORATION AND CONSOLIDATED SUBSIDIARIES
NOTES TO CONSOLIDATED STATEMENT OF INCOME — (Continued)

Note D:

The following inventory amounts were used in computing cost of products sold:

	December 31,					
	1975	1974*	1973*	1972	1971	1970
	Dollars in Thousands					
Finished goods	\$106,180	\$105,647	\$ 88,725	\$ 86,871	\$ 78,405	\$ 73,203
Work in process	46,329	43,948	36,694	36,359	33,368	33,755
Raw materials and supplies	78,432	99,865	59,449	48,280	44,631	39,948
Total	<u>\$230,941</u>	<u>\$249,460</u>	<u>\$182,868</u>	<u>\$171,510</u>	<u>\$156,404</u>	<u>\$146,906</u>

* Restated — See Note B.

Note E:

Extraordinary credits (charges) consist of the following (see Note H):

Year ended December 31, 1971:

Provision for estimated loss on disposal of certain plant facilities and related costs, less estimated reduction of state and local income taxes of \$477,000	\$(18,975,000)
Less estimated credits (provision) for United States income taxes and investment tax credit:	
Current	716,000
Deferred	8,570,000
Excess of investment tax credit recapture over unamortized deferred investment tax credit of \$804,000	(13,000)
Total	9,273,000
Estimated net loss	(9,702,000)
Other items — net (principally reversal of the excess portion of the 1969 provision for loss on disposal of facilities)	277,000
Total	(9,425,000)
Net gain on translation of foreign currencies (Notes B and 1)	992,000
Total	<u>\$ (8,433,000)</u>

The Company's chlorine-caustic operations were discontinued in September 1971, the ethylene oxide and CALSILITE® operations were discontinued in November 1971, and the related production facilities were disposed of in 1972. The estimated net loss and related costs resulting from the disposal of these facilities and an unused quarry, less a gain on the 1971 sale of certain woodlands, amounted to \$9,702,000 as shown in the above summary. The sale of the facilities in 1972 resulted in a loss which was \$20,000 greater than anticipated. This \$20,000 is included in costs and expenses in the 1972 Consolidated Statement of Income.

GAF CORPORATION AND CONSOLIDATED SUBSIDIARIES
NOTES TO CONSOLIDATED STATEMENT OF INCOME — (Continued)

Note E: — (Continued)

The following is a summary of the operating loss (see (a) below) of the discontinued operations:

	Year Ended December 31, 1971
	Dollars in Thousands
Net Sales	\$15,266
Cost of Products Sold	18,051
Directly Related Expenses	1,558
Total	19,609
Operating Loss(a)	<u>\$ 4,343</u>

(a) The Company reports its operations on the basis of responsibility accounting, whereby the various lines of business are measured after the assignment of only those items of income and expense for which each line of business is directly responsible. Accordingly, the operating loss as shown above is before the allocation of interest expense, the cost of certain functions that serve more than one line of business, miscellaneous expense and income items, and income tax effect.

Note F:

Interest is summarized as follows:

	Year Ended December 31,				
	1975	1974	1973	1972	1971
	Dollars in Thousands				
Interest on Long-Term Debt	\$13,408	\$ 9,296	\$ 8,746	\$ 7,718	\$ 8,218
Amortization of Debt Discount	198	164	68	42	43
Other Interest	2,949	7,332	3,254	2,477	2,098
Total	<u>\$16,555</u>	<u>\$16,792</u>	<u>\$12,068</u>	<u>\$10,237</u>	<u>\$10,359</u>

Note G:

During 1974, the Company relocated certain staff and administrative activities from its New York City offices to a new facility in Wayne, New Jersey. A reserve was established for costs anticipated to be incurred. The activity in the reserve has been as follows:

Original estimated reserve:

Present value of lease commitments in abandoned facility (less estimated sublease income) to be paid through March, 1983	\$3,000,000
Estimated employee relocation costs charged to income in first quarter, 1974	1,050,000
Provision for write-off of leasehold improvement	383,000
	<u>4,433,000</u>
Estimated employee relocation costs charged to income in second quarter, 1974	1,050,000
Original estimated relocation reserve	<u>5,483,000</u>

GAF CORPORATION AND CONSOLIDATED SUBSIDIARIES

NOTES TO CONSOLIDATED STATEMENT OF INCOME — (Continued)

Note G: — (Continued)

Balance from prior page		\$5,483,000
During the fourth quarter of 1974 the reserve was reduced as a result of the decision to continue utilization of a portion of the abandoned facility:		
Present value of lease commitments	\$(401,000)	
Leasehold improvements	(37,000)	(438,000)
Total relocation costs recorded in 1974		<u>5,045,000</u>
The reserve was reduced during 1974 for actual charges resulting from:		
Present value of rental payments (less sublease income)		(198,000)
Employee relocation costs		(1,840,000)
Write-off of leasehold improvements		(346,000)
Reserve balance at December 31, 1974		<u>2,661,000</u>
The reserve was reduced during 1975 for actual charges resulting from:		
Present value of rental payments (less sublease income)	\$(658,000)	
Employee relocation costs	(90,000)	
Alterations, commissions and other items	(148,000)	(896,000)
Provision for revised estimate of sublease income		<u>659,000</u>
Reserve balance at December 31, 1975		<u>\$2,424,000</u>

Note H:

During 1973, the Company curtailed the dyestuff and pigment operations at its Linden, New Jersey plant, resulting in a charge to income of \$5,942,000, including a write-off of \$4,992,000 of plant and equipment. Also during 1973, foreign exchange gains of \$1,830,000 were realized, principally as a result of the "devaluation" of the U. S. dollar.

The above items were included in Other Income (Charges) in the Consolidated Statement of Income for 1973, in accordance with Opinion No. 30 issued by the Accounting Principles Board during 1973. In 1971, similar items were presented as Extraordinary Items in conformity with then generally accepted accounting principles. Had Opinion No. 30 been in effect in 1971, Net Income for that year would have been the same, but Income Before Extraordinary Items would have been decreased by approximately \$8,433,000 (\$.62 per share — primary).

Note I:

The Company changed in 1971 to the equity method of accounting for an investment in a 49%-owned company, Chemical Developments of Canada, Limited (CDCL). The Company's equity in the earnings of CDCL, included in other income, amounted to \$533,000, \$610,000, \$191,000, \$240,000 and \$146,000 for the years ended November 30, 1975, 1974, 1973 and 1972 and the eleven months ended November 30, 1971, respectively.

GAF CORPORATION AND CONSOLIDATED SUBSIDIARIES
NOTES TO CONSOLIDATED STATEMENT OF INCOME — (Continued)

Note J:

The provision for income taxes consists of the following:

	Year Ended December 31,				
	1975	1974*	1973*	1972	1971
	Dollars in Thousands				
State	\$ 1,939	\$ 2,212	\$ 2,559	\$ 2,144	\$ 500
United States — current	10,558	15,692	13,789	14,057	10,167
United States — deferred	2,923	(755)	4,443	6,023	4,531
United States investment tax credit	(2,925)	(1,448)	(1,399)	(1,521)	(1,139)
Amortization of deferred United States investment tax credit arising prior to 1971	(573)	(591)	(591)	(608)	(689)
Foreign	3,641	5,926	4,984	2,548	2,356
Total Income Taxes	\$15,563	\$21,036	\$23,785	\$22,643	\$15,735

* Restated — See Note B.

MANAGEMENT'S DISCUSSION AND ANALYSIS OF THE CONSOLIDATED STATEMENT OF INCOME

1975 Compared with 1974

Consolidated sales increased \$15.6 million (2%) in 1975. Building Materials Group and Photo & Repro Group product sales increased \$11.7 million (3%) and \$5.9 million (2%), respectively. The increases resulted from higher prices on most major product lines partially offset by generally lower unit sales volumes.

Higher Building Materials Group sales were principally due to strong demand in the U.S. reroofing market. Increased Photo & Repro Group sales were largely the result of price increases and domestic graphic arts and printExpress® sales gains. Chemical Group sales decreased \$2.0 million (1%) to 235.1 million, reflecting depressed economic activity worldwide. Volumes declined for domestic felt and acetylene chemical products, more than offsetting significant sales gains in agricultural chemical products.

Costs of products sold for 1975 increased \$18.2 million (3%) primarily as a result of inflationary cost increases in all operating groups for most major raw materials, labor and plant operating costs.

Profits from both Chemical Group and Photo & Repro Group products were lower in 1975 than in 1974, reflecting lower unit sales and increased costs.

Total Other Income-Net of \$3.3 million was \$4.5 million better than last year due in part to a lower expense in other income (charges) — net of \$1.7 million which resulted from the favorable change in recorded foreign translation gains (losses) (after restatement — see Note B) and lower royalty expenses, partially offset by the nonrecurring profit in 1974 of \$1.4 million realized on the sale of three properties. In 1975 a nontaxable gain of \$4.0 million was realized on the sale of technology and know-how to the GAF/Hüls Chemie G.m.b.H. joint venture. In 1975 office relocation expenses of \$0.7 million were charged against income for costs associated with the 1974 move of certain administrative activities to Wayne, New Jersey. A similar provision of \$5.0 million in connection with such relocation was made in 1974.

Provision for 1975 income taxes decreased \$5.5 million (26%) due to a pre-tax income decline of \$3.0 million (6%) and an 8.9 percentage point decrease in the effective tax rate due primarily to the above noted \$4.0 million nontaxable gain, larger investment tax credits and greater benefits from exporting activities.

The effects of the accounting change for foreign translation gains (losses) (see Note B), as restated, in the Consolidated Statement of Income for the years 1975, 1974 and 1973 are as follows:

	Dollars in Millions				
	1975	Change	1974	Change	1973
Income Before Income Taxes and Extraor- dinary Items	\$ 3.5	\$10.0	\$(6.5)	\$(10.1)	\$ 3.6
Income Taxes	(1.8)	(4.3)	2.5	3.2	(0.7)
Net Income	<u>\$ 1.7</u>	<u>\$ 5.7</u>	<u>\$(4.0)</u>	<u>\$ (6.9)</u>	<u>\$ 2.9</u>

The effect for 1972 and earlier was immaterial.

1974 Compared with 1973

Consolidated sales for 1974 improved \$99.9 million (12%) over 1973. Price controls, in effect during the early months of 1974, delayed pass-through of inflationary cost increases in the Building Materials Group and the Chemical Group. On balance, price increases more than compensated for generally lower unit sales volumes (influenced by raw materials shortages) and were the principal contributor to improved sales results. The Photo & Repro Group, however, was unable to adequately recover increases in the costs of photographic products.

Costs of products sold for 1974 increased \$79.9 million (13%) from 1973, primarily as a result of inflationary cost increases in all operating groups for most major raw materials, labor and plant operating costs. Furthermore, raw material shortages in early 1974, the abrupt fourth quarter downturn in the economy, and cutbacks in production to reduce inventory levels, made it virtually impossible to keep manufacturing operations fully occupied, thereby having an unfavorable effect on profits. The increase was also attributable to the Company's adoption of LIFO accounting for dyestuffs and pigments inventories at its Rensselaer, New York plant.

Administrative and general expenses increased \$5.5 million (14%) in 1974 compared with 1973 as a result of higher staff operating expenses, including increased legal costs (\$1.4 million) and generally higher administrative costs consistent with inflationary trends.

Interest expense for 1974 increased \$4.7 million (39%) over 1973, as a result of record 1974 rates of interest and higher average levels of short-term borrowings.

Total Other Charges — Net for 1974 of \$1.2 million compares with \$4.3 million of income in 1973, due in part to the unfavorable change of \$5.9 million in other charges — net, which resulted primarily from the fluctuations in recorded foreign translation gains (losses), as restated. A \$5.5 million profit was realized in 1974 on the repurchase of 5% convertible subordinated notes in comparison with a similar profit of \$6.4 million in 1973. During 1973 the Company curtailed its Linden, New Jersey dyestuffs and pigments operations, resulting in a charge to income of \$5.9 million.

Provision for income taxes in 1974 declined \$2.7 million (12%) based upon the reduced level of income.

Maintenance and repair cost in 1974 increased \$5.3 million (15%) primarily as a result of the effects of double digit inflation in 1974 on the cost of upkeep of Company operations.

NINE MONTHS (UNAUDITED) CONSOLIDATED FINANCIAL STATEMENTS

All adjustments necessary to a fair statement of the results for the nine months ended October 3, 1976 and September 28, 1975 have been included. All such adjustments are of a normal recurring nature.

GAF CORPORATION AND CONSOLIDATED SUBSIDIARIES

(UNAUDITED) CONSOLIDATED STATEMENT OF INCOME

Nine Months Ended October 3, 1976 and September 28, 1975

	Nine Months Ended	
	(Dollars in Thousands Except Per Share Amounts)	
	October 3, 1976	September 28, 1975
		(Note b)
Net Sales	\$812,300	\$711,308
Costs and Expenses:		
Costs of products sold	594,238	509,181
Distribution and selling	110,602	98,642
Advertising	14,696	13,011
Research and development	12,811	11,303
Administrative and general	38,085	34,327
Interest	11,929	12,865
Total Costs and Expenses	780,361	679,329
Other Income:		
Gain on sale of technology and know-how (note a)	—	4,000
Other — net	639	3,580
Total Other Income — net	639	7,580
Income Before Income Taxes	32,578	39,559
Income Taxes	13,711	13,587
Net Income	18,867	25,972
Less preferred stock dividend requirements	2,727	2,726
Earnings applicable to common stock	\$ 18,140	\$ 23,246
Earnings per common share:		
Primary	\$1.21	\$1.76
Fully diluted	\$1.09	\$1.51
Cash Dividends Declared:		
Per preferred share	\$.90	\$.90
Per common share	\$.43	\$.39
Weighted Average Number of Common Shares Outstanding (in thousands) ..	13,309	13,222

See Notes to (Unaudited) Consolidated Financial Statements.

GAF CORPORATION AND CONSOLIDATED SUBSIDIARIES

(UNAUDITED) CONSOLIDATED BALANCE SHEET

ASSETS	October 3, 1976	September 28, 1975
		(Note b)
	(Dollars in Thousands)	
Current Assets		
Cash	\$ 23,909	\$ 24,890
Accounts receivable — less allowance for doubtful accounts — 1976, \$6,234,000; 1975, \$4,791,000	196,640	188,555
Inventories		
Finished goods	111,817	102,168
Work in process	51,779	50,162
Raw materials and supplies	85,998	73,885
Total Inventories	249,594	226,245
Prepaid expenses	7,828	6,739
Total Current Assets	477,971	446,438
Property, Plant and Equipment	433,446	406,206
Less Accumulated Depreciation	177,838	166,660
Property, Plant and Equipment — net	255,608	239,546
Cost in Excess of Net Assets Acquired	34,737	34,956
Other Assets	16,593	15,862
TOTAL ASSETS	\$784,909	\$736,822
LIABILITIES AND STOCKHOLDERS' EQUITY		
Current Liabilities		
Notes and accounts payable	\$143,931	\$ 81,388
Current portion of long-term debt	2,392	7,186
Accrued liabilities	45,117	48,333
United States and foreign income taxes	10,764	12,129
Total Current Liabilities	202,204	149,036
Long-Term Debt less Current Portion	146,316	170,832
Deferred Taxes and Other Liabilities	46,544	40,253
Stockholders' Equity		
Preferred stock at assigned value of \$1.25 per share	3,882	3,882
Common stock at \$1 par value	13,771	13,764
Additional paid-in capital	53,494	53,016
Retained earnings	323,997	311,202
Total	395,144	381,864
Less stock held in treasury, at cost:		
Preferred — 1976, 76,400 shares; 1975, 76,400 shares	932	932
Common — 1976, 534,099 shares; 1975, 525,949 shares	4,367	4,331
Total Stockholders' Equity	389,845	376,601
TOTAL LIABILITIES AND STOCKHOLDERS' EQUITY	\$784,909	\$736,822

See Notes to (Unaudited) Consolidated Financial Statements.

GAF CORPORATION AND CONSOLIDATED SUBSIDIARIES
(UNAUDITED) CONSOLIDATED STATEMENT OF CHANGES IN FINANCIAL POSITION

	<u>Nine Months Ended</u>	
	<u>October</u>	<u>September</u>
	<u>3, 1976</u>	<u>28, 1975</u>
	(Note b)	
	(Dollars in Thousands)	
Funds Provided		
From Operations		
Net income	\$ 18,867	\$ 25,072
Depreciation	19,874	18,550
Other	4,115	3,525
Funds provided from operations	42,856	48,047
Issuance of Long-Term Debt	77,458	499
Other	91	580
Total	<u>120,405</u>	<u>49,126</u>
Funds Applied		
Additions to Property, Plant & Equipment	32,819	27,773
Cash dividends	8,416	7,878
Reductions in Long-Term Debt	70,396	10,037
Investment in Joint Venture Company	—	6,549
Other	835	3,780
Total	<u>112,466</u>	<u>56,017</u>
Increase (Decrease) in Working Capital	<u>\$ 7,939</u>	<u>\$ (6,891)</u>

See Notes to (Unaudited) Consolidated Financial Statements.

CAF CORPORATION AND CONSOLIDATED SUBSIDIARIES

NOTES TO (UNAUDITED) CONSOLIDATED FINANCIAL STATEMENTS

All adjustments necessary to a fair statement of the results for the nine months ended October 3, 1976 and September 28, 1975 have been included. All such adjustments are of a normal recurring nature.

Note a: During 1975 the Company and Chemische Werke Hüls, A.G. ("Hüls"), a West German company, formed a joint venture (CAF/Hüls Chemie G.m.b.H.) to construct and operate a butanediol manufacturing plant in West Germany. The joint venture is owned equally by the Company and Hüls. The investment is included in Other Assets and has been accounted for by the equity method.

In the second quarter of 1975, the Company sold certain technology and know-how to the joint venture resulting in a gain of \$4,000,000. This gain is not subject to U.S. income tax.

Note b: Previously reported results for the first nine months of 1975 have been restated to reflect a change in the method of accounting for foreign currency translations to comply with a statement issued by the Financial Accounting Standards Board in late 1975. The effect of the restatement was to increase previously reported net income for the first nine months of 1975 by \$3,716,000 (\$.28 per share — primary; \$.22 per share — fully diluted).

Note c: The following is a summary of 1976 quarterly results:

	1976 — By Quarter		
	Third	Second	First
	(Dollars in Thousands Except Per Share Amounts)		
Net Sales	\$282,163	\$271,662	\$258,475
Cost of Products Sold	208,795	194,869	190,574
Gross Profit	73,368	76,793	67,901
Net Income	\$ 5,911	\$ 8,176	\$ 4,780
Earnings per Common Share:			
Primary	\$.37	\$.55	\$.29
Fully Diluted	\$.34	\$.47	\$.28

**MANAGEMENT'S DISCUSSION AND ANALYSIS OF
NINE MONTHS (UNAUDITED) CONSOLIDATED FINANCIAL STATEMENTS**

Consolidated sales increased \$101.0 million (14%) as compared with the same period in 1975, due largely to higher domestic volume in all product groups and selling price increases in the Building Materials group. There were four more billing days in the first nine months of 1976 than in 1975. Worldwide product sales groups net sales were as follows: Building Materials up \$49.4 million (18%) to \$328.3 million; Chemical up \$30.3 million (17%) to \$203.9 million; Photo & Repro up \$21.3 million (8%) to \$280.1 million. All of the Company's major product lines except agricultural chemicals, consumer photo, and floor tile products showed volume increases. International sales were up \$6.4 million (5%) to \$128.6 million, but were restricted by the effects of currency movements and to a lesser extent the slower economic recovery abroad.

Total costs and expenses were \$101.0 million, 15% higher than the same period last year. Cost controls and greater utilization of facilities were offset by the effects of inflation. Interest expense declined \$0.9 million (7%) due to a lower level of total debt during most of the first half of 1976.

The category of Other Income Other — net was unfavorable by \$3.0 million due to foreign exchange losses in 1976 compared with gains in 1975.

Net income decreased \$7.1 million (27%) in the first nine months of 1976 as compared with the same period in 1975. However, the 1975 income includes a nontaxable, nonrecurring \$4.0 million gain on sale of technology and know-how. Foreign currency fluctuations decreased net income in 1976 as compared with 1975 by \$6.5 million. The decrease arose principally from foreign exchange transactions and the application of Financial Accounting Standard No. 8 to inventories.

Earnings from domestic operations increased on overall higher unit sales volumes. Although all domestic groups contributed to the volume increase, only the Chemical operations (notwithstanding the significant decline in sales of agricultural chemicals, a high profit margin product line) gained sufficient volume to offset substantially the net cost increases. The Building Materials operation experienced a slight decline in earnings from last year's level, which reflects a third quarter softness in the building materials market, increased price competition, and a production cutback to reduce inventories. The Photo & Repro operation results improved somewhat but continue to reflect an overall softness in this group. The International results declined due to continued weaknesses in some foreign economic conditions and the above mentioned effect of foreign exchange. Preliminary figures available to date for the fourth quarter indicate that for 1976 the domestic and international operations of the Photo & Repro group, on a combined basis, will probably show a direct operating loss (which is before unallocated corporate and interest expenses).

The effective tax rate for 1976 increased to 42.1% from 34.3% in 1975 primarily as a result of the nontaxable \$4.0 million gain and a higher expected annual tax rate.

PRICE RANGE OF COMMON STOCK; DIVIDENDS

The table below shows for the indicated periods the high and low sales prices of the Common Stock on the New York Stock Exchange through January 23, 1976 and on the Consolidated Tape Network A thereafter, and dividends paid on the Common Stock. All price information contained in the table below was obtained from the National Quotation Bureau, Inc.

	Sales Prices		Dividends per Share
	High	Low	
1971	\$24½	\$12¾	40¢
1972	27	19¾	40
1973	22¼	8¼	42
1974			
First Quarter	11½	8¾	11
Second Quarter	10½	8½	11
Third Quarter	8¾	6	11
Fourth Quarter	8¾	6½	13
1975			
First Quarter	11½	7½	13
Second Quarter	12½	9¼	13
Third Quarter	13¼	9½	13
Fourth Quarter	11¾	9½	13
1976			
First Quarter	17½	10¾	13
Second Quarter	16¾	13½	15
Third Quarter	16¾	13¾	15
Fourth Quarter (through December 21)	14½	11	15

Future dividends on the Common Stock will necessarily be dependent upon future earnings, the financial needs and condition of the Company, and other factors. See "Description of Capital Stock" for information as to certain limitations on the payment of dividends.

DESCRIPTION OF BUSINESS

The Company is engaged in three lines of business: the manufacture and sale of (i) chemicals; (ii) photographic and reprographic products; and (iii) building materials.

The Company reports its operations on the basis of responsibility accounting, whereby the various product sales groups are measured after the assignment of only those items of income and expense for which each product sales group is directly responsible. Accordingly, the Company does not provide for the allocation of interest and other debt expense, the cost of certain functions that serve more than one product sales group, and miscellaneous expense and income items.

The following table sets forth for the periods indicated (i) net sales and (ii) direct operating profit of the product sales groups of the Company.

	(Unaudited) Nine Months Ended		Year Ended December 31,				
	October 3, 1976	September 28, 1975	1975	1974(a)	1973(a)	1972	1971
	Dollars in Thousands						
Net Sales							
Chemical	\$203,885	\$173,609	\$235,115	\$237,099	\$215,317	\$193,595	\$177,288
Photo & Repro	280,140	258,829	356,994	351,111	330,190	296,296	260,407
Building Materials	328,275	278,870	372,312	360,599	303,379	278,569	246,067
Total	<u>812,300</u>	<u>711,308</u>	<u>\$964,421</u>	<u>\$948,809</u>	<u>\$848,886</u>	<u>\$768,460</u>	<u>\$683,762</u>
Direct Operating Profit							
Chemical	31,612	27,308	\$ 36,154	\$ 45,661	\$ 20,790(b)	\$ 24,475	\$ 24,334
Photo & Repro	314	3,127	4,820	9,951	18,256	11,468	7,403
Building Materials	36,786	38,294	48,795	43,555	38,811	48,005	44,442
Total	<u>63,712</u>	<u>68,727</u>	<u>89,769</u>	<u>99,167</u>	<u>86,857</u>	<u>83,948</u>	<u>76,179</u>
Operating Loss of Discontinued Operations	—	—	—	—	—	—	(4,343)
Interest Expense	(11,929)	(12,865)	(16,555)	(16,792)	(12,068)	(10,237)	(10,359)
Unallocated Corporate Expense — Net	<u>(24,205)</u>	<u>(16,303)(c)</u>	<u>(26,705)(c)</u>	<u>(32,822)(d)</u>	<u>(19,185)(c)</u>	<u>(23,362)</u>	<u>(23,835)</u>
Income before Income Taxes and Extraordinary Items	<u>\$ 32,578</u>	<u>\$ 39,559</u>	<u>\$ 46,509</u>	<u>\$ 49,553</u>	<u>\$ 55,604</u>	<u>\$ 50,349</u>	<u>\$ 37,642</u>

(a) Restated for accounting change. See Note B to Consolidated Statement of Income.

(b) Includes \$5,942,000 charge for phase-out of Linden dyestuff and pigment operations. See Note H to Consolidated Statement of Income.

(c) Includes \$6,359,000 gain on the reacquisition of 5% Convertible Subordinated Notes.

(d) Includes \$5,523,000 gain on the reacquisition of 5% Convertible Subordinated Notes and a charge of \$5,045,000 for office relocation expenses. See Note G to Consolidated Statement of Income.

(e) Includes \$4,000,000 gain on sale of technology and know-how. See Note A to Consolidated Statement of Income.

The principal products, sources of supply, market position and recent developments with respect to the Company's three product sales groups are as follows:

Chemical

Products

The chemical product sales group includes the following: *Dyestuffs and Pigments* — The Company's line of dyestuffs is primarily used in the textile and paper industries and also in the leather industry; its organic pigments are used for coloring many different products, including rubber, plastics, printing inks, lacquers and natural and synthetic textiles. *Surface-active agents* — Surface-active agents (or surfactants) possess detergent, emulsifying, dispersing and wetting properties and are used in

the manufacture and compounding of detergents (primarily industrial), insecticides, pesticides, textiles, paper, leather, rubber, plastics and chemicals and in the production and refining of petroleum and mineral products. *High-Pressure Acetylene Derivatives* — The Company has developed and employs techniques for processing acetylene, a very explosive gas, under high pressure into a wide variety of acetylene derivatives, with uses in the manufacture of plastics, synthetic fibers, cosmetics, electroplating chemicals, pharmaceuticals, solvents and adhesives. *Specialty and Textile Chemicals* — These include bactericides and fungicides, brighteners, leather tanning and finishing agents, textile treating chemicals, flame retardants, ultraviolet absorbers, solvents, carbonyl iron powders and silver salts. *Industrial Organic Chemicals* — These compounds are used in the production of surfactants, dyestuffs, pharmaceuticals, defoliants, herbicides, growth regulators and other agricultural chemicals, plastic stabilizers, electroplating chemicals, and photosensitive and other chemicals. *Latex Products* — These products include rubber and polymer lattices for rug backings, fabric coatings and paper coatings; latex foam backing for drapery fabrics; and latex adhesives for fabric lamination. *Other Industrial Products* — These products include roofing granules, wool pressed felts, FEUTRON® (a line of needled felts), synthetic fiber felts, papermakers felt and GAFLO® (a line of filter products).

The Company's chemical products are sold to users principally by its own sales personnel and, in some cases, by independent distributors.

Raw Materials and Supplies

The raw materials used in the production of the Company's chemical products are purchased from a large number of outside sources, in many cases pursuant to supply contracts which are, in general, standard for the industry. Certain of the Company's raw materials, including acetylene, are obtained from single or limited sources pursuant to supply contracts. With respect to acetylene, which is supplied to the Company at two locations by separate sources, were either of the sources to be discontinued the development of alternate sources of supply could involve interruption of production and would probably result in substantially increased costs.

Petroleum-based products are used in many of the Company's chemical manufacturing processes and consequently the price and availability of petroleum is material to the costs of operations.

Although this product sales group has from time to time in the past experienced difficulty in obtaining adequate supplies of raw materials, particularly during 1974, it has not experienced any significant shortages of raw materials since the beginning of 1975.

Market Position

The Company is the sole United States producer of a complete line of high-pressure acetylene derivatives, although it competes with foreign manufacturers. Only one of these foreign manufacturers is an important factor in the domestic market and it is currently completing construction of a plant in the United States for the production of butanediol, a major product in the high-pressure acetylene chemical line. Another large domestic chemical manufacturer has made sales of butanediol in the United States. The Company believes it is a major supplier in the wool and synthetic fibre felts industries.

In the balance of its chemical business the Company faces competition from many companies, certain of which are substantially larger than the Company and offer a broader range of products. The Company believes that the great size and diversified nature of the chemical industry make it impossible to give a meaningful estimate of the relative position of the Company in this field.

Recent Developments

In early 1975 the Company entered into an agreement with Chemische Werke Hüls, A. G. ("Hüls") to construct and operate a butanediol manufacturing plant in Marl, West Germany, with a planned annual capacity of approximately 60 million pounds. The Company anticipates that this plant will permit it to compete effectively with the manufacturer which currently dominates the European butanediol market. The plant will be owned and operated by a German joint venture company owned in equal shares by Hüls and the Company; production is planned to begin in late 1977. The agreement also includes provision for Hüls to supply acetylene to the plant from its adjacent manufacturing plant. The Company anticipates that the joint venture company will require approximately \$24,000,000 in loans, in addition to the \$12,000,000 in cash it has already received as capital contributions, for completion of the plant. It is expected that these loans will be obtained from third parties on the credit of the joint venture company, but the Company and Hüls may share equally in providing loans or guarantees of loans if necessary.

During 1975, the agrichemical business was responsible for significant profits for the Company. Sales of agrichemical products, which the Company manufactures on a contract basis to the specifications of large purchasers, have substantially declined during the first nine months of 1976 with resulting adverse effects upon earnings, and a continuing erosion of the level of sales and earnings is anticipated. With respect to one of these products, COBEX®, the purchaser has given notice to the Company that it is terminating its agreement to purchase, effective March 13, 1977. With respect to another such product, AMIBEN®, the purchaser, Amchem Products, Inc. ("Amchem"), has indicated to the Company that purchases of AMIBEN® will continue for the current growing season at a sharply reduced level from 1975 levels. Amchem has also given the Company notice that, effective December 31, 1976, it is terminating the contract pursuant to which the Company has been supplying Amchem with 2-chloroethylphosphonic acid (ethephon). The Company continues to market ethephon to consumers. See "Litigation and Other Matters". The herbicide Oryzalin had been manufactured by the Company for Eli Lilly and Company under an agreement which expired by its terms on June 30, 1976.

The Company has under construction a facility at its Calvert City, Kentucky plant for the manufacture of polybutylene terephthalate ("PBT"). Construction of such facility is expected to be completed during 1977. PBT is the basic material for a family of polyester resins which possess properties suitable for use in the automotive and electronics markets, among others. While the Company is one of a small number of companies which produce butanediol, one of the basic raw materials for PBT resin, substantial competition in the various PBT markets from a number of other manufacturers, certain of which are substantially larger than the Company, is anticipated. The plant discussed above under "Market Position", which is being completed by a foreign manufacturer, will produce butanediol.

The wool felt industry has experienced overcapacity for a number of years, principally because the total demand for wool felt has been declining. The Company is contemplating consolidating certain of its wool felt manufacturing operations.

See Note E to the Consolidated Statement of Income for the effect of discontinuance of chlorine-caustic and ethylene oxide operations. See "Litigation and Other Matters" for a discussion of pending litigation between the Company and Amchem. Union Carbide Corporation has announced an agreement in principle to acquire Amchem. The Company is unable to predict what effect, if any, this acquisition may have on such litigation or sales to Amchem.

Photo & Repro

Products

The photographic and reprographic product sales group includes the following: *Consumer Photo Products*—including color and black-and-white film (print film, slide film and movie film), still and motion picture cameras and projectors, slide viewers and scenic slide and print assortments, and VIEW-MASTER® and TALKING VIEW-MASTER® stereo reels, viewers and projectors; *X-ray Products*—including x-ray film and developing chemicals for medical, dental and industrial use; *Graphic Arts Products*—including film, film bases, and chemicals used in photolithography, rotogravure printing, offset printing, photographic typesetting and photoengraving; *Industrial Products*—including film and paper employed in oscillograph recording, mapping and tracing; *Professional Photography Products*—including black-and-white and color still film, and photographic papers for professional photographic applications, press and industrial photography and professional portraiture; and *Reprographic Business Systems Products*—including diazo reproduction equipment, sensitized reproduction materials used in such equipment, business forms, micrographic equipment and supplies, sensitized paper and toner for electrostatic office copiers, and drafting office supplies.

The Company also offers consumer photo finishing services through 19 photofinishing plants in the United States and Europe.

Distribution of the Company's consumer and professional photo products is made through a field sales force consisting in part of the Company's own employees and in part of independent sales representatives or distributors. Sales are primarily to mass merchandisers and to photo specialty shops. The Company's graphic arts and x-ray photo products are sold in part to distributors, and in part, along with other industrial photo products, directly to users. The reprographic business systems products are sold in part directly by the Company's own employees and in part through independent dealers. The reprographic machines sold by the Company are serviced in part by the Company's own employees and in part by employees of such independent dealers who are trained by the Company.

Raw Materials and Supplies

The Company purchases from several sources the raw materials and components (some of which are manufactured pursuant to its specifications) for the film, paper, slide and motion picture projectors and viewers manufactured by it. The price of silver, which is one of the more important raw materials used in the manufacture of film and photographic paper, has risen sharply since 1972. The price of silver, based on the Handy & Harman daily New York quotations, ranged from \$1.387 to \$2.048 per troy ounce in 1972, from \$1.962 to \$3.28 per troy ounce in 1973, from \$3.27 to \$6.70 per troy ounce in 1974, from \$3.91 to \$5.225 per troy ounce in 1975, and from \$3.815 to \$5.10 per troy ounce in 1976 through December 1. In each of these years, except 1976, the cost of silver used in the Company's manufacturing operations was higher than in the preceding year. Competitive factors have limited and still limit the Company's ability to implement price increases related to this increased cost. Accordingly, the increased cost of silver may continue to have a material adverse effect on the earnings of the Company unless substantial price increases can be effected or the price of silver declines.

The still and motion picture cameras and sound projectors sold by the Company are manufactured specially for the Company by companies located in Japan, Hong Kong, Macao and Taiwan. Efforts by the Company are underway to commence purchases from a number of additional suppliers. During

1976 the Company has been experiencing unusual delays in obtaining these supplies which has adversely affected sales.

Acetate film base used by the Company is manufactured by it. Other film bases, including polyester, and raw paper are purchased from domestic and foreign sources.

The raw materials and supplies used in the manufacture of reprographic business products are purchased from several sources and, although in some cases parts are built to the Company's specifications, alternate sources for such parts are available.

Market Position

The photographic industry is dominated in many areas by Eastman Kodak Company ("Eastman"). The Company's small share of the market also faces competition from foreign sources. In general, the Company offers a broad range of photographic products, which is, however, considerably narrower than that offered by Eastman. The Company believes it is the leading producer of stereo viewers and reels.

The Company has initiated litigation against Eastman, which is more fully described below. A favorable decision in that suit could have a beneficial effect on the Company's photographic business, however, an adverse decision could result in the continuation of the present adverse competitive position of the Company and have significant implications concerning the future of the Company in various aspects of the photographic business. The outcome of the litigation cannot be predicted at this time.

The Company believes that it is one of the two leading domestic producers of diazo reproduction equipment and diazo papers, plastic films and other diazo-coated products. The diazo reproduction process, while suitable for copying engineering and architectural drawings because of its capacity to make larger copies, is limited in general applicability by the need for a translucent master sheet printed only on one side. The diazo process may be subject to increasing competition from other processes and may become subject to increased regulation. See "Environmental Control and Related Matters".

The field of business forms produced pursuant to customer specifications is dominated by another company. The business forms products of the Company are sold principally in the northern part of the United States east of the Mississippi River.

Recent Developments

Since 1973 the direct operating profit (without allocation of interest expense and unallocated corporate expense) of the Photo & Repro Group has declined sharply, and in 1976 the group will probably show a direct operating loss. This decline on a worldwide basis has been the result of a number of factors affecting photographic products, including, significantly, the introduction of products by Eastman rendering competitive products obsolete, as well as increases in the price of silver and other cost increases which have not been passed on in full, and general economic conditions affecting both consumer and industrial markets. Moreover, the Company has been required to incur for its photographic line of products, advertising costs, research and development expenses, and working capital requirements disproportionately greater than the contribution of the Photo & Repro Group to the Company's sales.

The 1972 introduction of Eastman's C-41 film and the conversion by photo finishers to the different processes required to develop such film has had, and is expected to continue to have, the effect of substantially curtailing the developing of the Company's C-22 color print film by photo finishers and has thereby reduced, and may be expected to continue to reduce, demand for such film. The Company's photo finishing plants retain the capacity to develop and process both the Company's C-22 film and Eastman's C-41 film, and the Company expects to retain the capacity for developing and processing its C-22 film so long as there is sufficient demand.

Since the introduction of Eastman's C-41 film, the Company has had under development a new color print film for pocket-sized instant loading cameras, standard size instant loading cameras and 35 millimeter cameras which could be developed with the same chemicals used in developing Eastman's C-41 film and other subsequently introduced competitive films. The Company is making limited shipments of the new film for pocket-sized instant loading cameras and is making preparations for commercial production of the new film in 1977. However, no assurance can be given that this objective will be reached.

On April 30, 1973, the Company filed an antitrust action against Eastman in the U.S. District Court for the Southern District of New York seeking treble damages in an unstated amount and certain equitable relief, including the division of Eastman into ten separate and independent businesses, the dedication to the public of the trademark "Kodak" and disclosure and licensing on a royalty-free basis of all Eastman's present and future photographic patents and know-how.

The Company stated in its Complaint that it is the last remaining domestic competitor to Eastman in the manufacture of conventional amateur photographic film. The Company alleged that Eastman has forestalled innovation in the development of products incompatible with those of Eastman, and has made numerous changes in its products in order to make the products of its competitors unmarketable. The Complaint further alleged that Eastman has, in many areas of the photographic industry, monopolized the production and sale of photographic supplies, restrained trade, foreclosed markets, made illegal acquisitions and engaged in various other illegal acts and practices. Eastman filed an Answer denying the material allegations of the Complaint. Document discovery and oral depositions of witnesses are underway in the pre-trial proceedings, and a trial date has been tentatively set for early 1978.

The Company's film, under an agreement which expired October 1, 1976, has been the official film of Disneyland and Walt Disney World, where the Company has Photo Exhibit Centers and the Company's photo products, together with certain products of other manufacturers, have been sold through more than 50 retail photo outlets. The Company has recently obtained an extension to September 30, 1979 of this agreement pursuant to which additional photographic products not produced by the Company may be sold.

The Company's \$9 million expansion of its photo product facilities in Sint-Niklaas, Belgium, announced in 1974, is scheduled to be completed in December 1976. The agreements relating to the development and financing of this project require that the Company have certain minimum numbers of employees at various times which would represent additions to the current work force. If present business conditions continue, however, it is expected that this plant will operate at substantially less than full capacity.

An investigation by British authorities of certain practices, including pricing, of the members of the diazo industry in the United Kingdom, including the Company's British subsidiary, is under way.

It is not anticipated that such investigation will generate a materially adverse result insofar as the operations either of the British subsidiary or the Company are concerned.

The largest single customer for the Company's color print film has advised the Company that it will be unable to make current payments with respect to approximately \$3 million of the Company's accounts receivables and has requested a one year moratorium with respect to such payments. A substantial portion of such customer's indebtedness is secured by a second mortgage on certain property of the customer.

On December 22, 1976 the Company purchased the medical products division of United States Radium Corporation for a price of approximately \$2.5 million. The division manufactures x-ray intensifying screens, cassettes and related hardware.

Building Materials

Products

The building materials product sales group includes the following: asphalt shingles; built-up roofing, consisting of organic and asbestos-based felts; asphalt roof coatings and plastic cements; organic and asbestos dry felt produced primarily for use by the Company's roofing or flooring plants; vinyl siding; mineral fiber roof shingles and siding; mineral fiber building board; mineral fiber canal bulkhead designed and processed to prevent land erosion by either salt or fresh water; vinyl asbestos floor tiles; vinyl sheet floor coverings; automotive sound deadening and insulation products; and adhesives, cove bases and glass fiber insulation (each purchased for resale).

The Company sells its products through its own salesmen to wholesalers, retailers, applicators, contractors and builders. Such sales are mostly limited, in the case of building materials other than floor tiles and sheet vinyl, to states east of the Rocky Mountains. Its products are also supplied, on a bid basis, to United States and State agencies. The Company operates its own distribution outlets for resilient flooring in six cities where available outlets were not deemed satisfactory.

Raw Materials and Supplies

A major portion of the raw materials used for the manufacture of building materials is purchased from a large number of outside sources and the balance is produced by the Company, including roofing granules, which are used to surface asphalt roofing products.

Raw material ingredients for dry felt, which have been in good supply, are rags, waste paper, pulpwood and wood flour, purchased in the open market at prices which are subject to fluctuation. Asphalt is purchased from major oil refineries and independent operators, in one case pursuant to a long term supply contract. The Company purchases glass fiber insulation from a single source which has allowed its long-term supply contract for residential building insulation with the Company to lapse and has advised that it intends to cease to supply the Company's requirements. The Company is contesting this position, and discussions are currently underway with this supplier.

During 1975 the Company experienced difficulty in obtaining sufficient quantities of asbestos for use in the felt components of roofing and flooring products, resulting in lowered production of roofing and flooring products in the last half of 1975. Although asbestos is presently more readily available, limited shortages continue to exist.

Market Position

The building materials industry is highly competitive. The Company believes that it is one of the leading producers of asphalt roof shingles, built-up roofing, mineral fiber roof shingles, siding shingles, mineral fiber flat sheets, vinyl floor coverings, vinyl siding and automotive sound deadening and insulation products. One of the Company's largest customers for roofing materials has announced its intention to begin producing its own materials.

Recent Developments

Roofing products constitute the major portion of total sales of the building materials product sales group. It is believed that historically a majority of roofing products sold by the Company have been used in reroofing of existing structures. It is reported that housing starts were at a level of approximately 2,379,000 units in 1972, 2,058,000 units in 1973, 1,353,000 units in 1974, 1,171,000 units in 1975, and 1,500,000 units (estimated) in 1976. Despite the consistent decline in reported housing starts between 1972 and 1975, the Company's sales revenues from roofing products increased in 1973, 1974 and 1975 over the then prior years, although unit sales (which increased in 1973 and 1974 over the then prior years) decreased in 1975 from the record unit sales recorded by the Company in 1974.

In 1975 and 1976 the Company concluded initial arrangements for the construction of a sheet vinyl flooring plant in Mullingar, Ireland. Construction is presently scheduled to be completed in late 1977. The plant will be owned and operated by GAF (Ireland) Company, a branch of GAF (Nederland) B.V. ("GAF Nederland"), a wholly-owned subsidiary of the Company, and will be the Company's principal source of sheet vinyl for sale in Europe and other overseas markets. The Company anticipates that it will face substantial competition for its sheet vinyl products in the European market in view of competitors' recently announced plans for increased capacity to serve that market.

The Company anticipates that capital expenditures on the plant will be in excess of \$33 million. Estimates of the total cost of the project have been, and are expected to continue to be, influenced by fluctuations in exchange rates and inflation in Ireland. Arrangements have been concluded with the Industrial Development Authority of Ireland to obtain grants for a portion of the cost of the project, provided that the Company makes equity investment in the project at least equal to the aggregate amount of the grants. Such investment, and other funds necessary for completion and operation of the project, may be obtained by the Company through loans made to the Company and/or GAF Nederland. The Company has arranged with Irish and English banks to borrow portions of the required funds. The Company will provide additional capital for completion and operation of the project from the Company's general funds and/or domestic lending sources.

As a result of the settlement in May 1970 of a lawsuit commenced in 1966 against The Ruberoid Co., the Company entered into a license agreement with Congoleum Industries, Inc. whereby the Company was licensed to manufacture and sell foamed vinyl flooring which uses a chemical embossing process. In exchange for such license, the Company agreed to pay a royalty equal to 5% of the net sales of such product during the term of the agreement, which has a stated term ending on December 20, 1983, and, in any event, the Company is required to pay a minimum royalty of \$125,000 a year through 1983, which amount is applied against royalties payable in each such year. Royalties paid under this agreement for 1972, 1973, 1974 and 1975 amounted to approximately \$1,023,000, \$905,000, \$719,000 and \$466,000, respectively.

International Operations

The Company's international operations, which are consolidated in the net sales and income for the Company's three lines of business and product groups, include export of the products manufactured by the Company in the United States (principally its sheet vinyl, acetylenes, industrial photographic and consumer photographic products) and the operations of the Company's foreign subsidiaries. Sales by foreign subsidiaries are principally in Western Europe. Subsidiaries are also active in Australia, Canada and elsewhere. For 1973, 1974 and 1975, the Company's international operations, including export sales from domestic operations, accounted for approximately 16%, 17% and 17%, respectively, of its net sales for such years.

In general, during 1973, 1974 and 1975, the ratio of operating profit to sales in international operations exceeded such ratio in domestic operations, and international operating profits in 1973 were almost double those of 1972. However, in the first nine months of 1976 due to economic conditions in Europe and the effect of foreign exchange fluctuations, the ratio in international operations did not exceed such ratio in domestic operations. See Note 2 of Notes to Consolidated Financial Statements for information as to foreign operations included in international operations. See pages 23, 20 and 25, respectively, for discussions of expansion of the Company's European photo product facilities, construction of a new chemical manufacturing plant in West Germany, and construction of a new sheet vinyl manufacturing facility in Ireland.

New Business Venture

On June 7, 1976 the Company's wholly-owned subsidiary, GAF Broadcasting Company, Inc., acquired New York City radio station WNCN-FM for the sum of \$2,200,000. WNCN gained national attention in late 1974 when it changed its programming and discontinued playing classical music. WNCN has subsequently returned to a classical music format. The Company has budgeted additional capital expenditures for the construction of a new broadcasting complex and the improvement of the station's transmitting quality.

Research and Development

Research and development expenses in 1974 and 1975 were \$15,011,000 and \$15,272,000, respectively. Approximately 65% of the amount spent in 1975 was used for research to develop new or improved products and processes, while the remaining 35% was for improvement of existing products and technologies. The latter category includes product quality improvements, improved formulations, and experimentally-developed new applications data to exploit the full potential of existing company products. During 1974, approximately 60% of research and development expenses were used for the development of new products and processes, while approximately 40% was used to enhance existing products and technologies.

As of October 31, 1976, 280 professional employees were engaged in Company-sponsored research and development.

During 1972 the Company relocated several research and development functions to Wayne, New Jersey. See "Facilities" for further details concerning the Wayne site.

Employees

At October 31, 1976 the Company employed approximately 21,000 people, which number is expected to be reduced by approximately 2.5% pursuant to a Company-wide cost reduction program presently in progress. At such date, approximately 8,400 employees in the United States and Canada were represented by 69 unions under contracts which are effective, in most cases, for two or three year periods. Employee relations at all of the Company's plants have been generally satisfactory. In 1975 work stoppages related to contract renewal negotiations occurred at the following facilities of the Company for the respective periods of time indicated: (a) Baltimore, Maryland roofing plant — one month; (b) Whitehall, Pennsylvania sheet vinyl plant — four days; (c) Long Beach, California floor tile plant — three weeks; and (d) Annapolis, Missouri granules quarry — one month. During 1976 a three week stoppage occurred at the Company's San Francisco distribution facility and a one week stoppage at the Binghamton, New York photographic products plant. The Company has in effect various benefit plans which include retirement plans and group insurance arrangements providing life, accident, hospital, surgical and medical coverage. The Company and, in most cases, the employees contribute to the costs of the insurance arrangements. See Notes 1 and 9 of Notes to the Consolidated Financial Statements for further details concerning the retirement plans.

Patents

The Company owns approximately 1,750 domestic and 1,900 foreign patents and approximately 900 domestic and 2,650 foreign trademarks, and is licensed under many other United States and foreign patents, no one or group of which is deemed to be material to the conduct of the Company's business as a whole other than the patents covered by the licenses from Congoleum Industries, Inc. and Amchem described under "Building Materials — Recent Developments" and "Chemical — Recent Developments," respectively, and a group of patents on photographic products and processes for making photographic film covered by licenses from Eastman, which patents have been challenged by the Company in the antitrust action against Eastman described under "Photo & Repro — Recent Developments."

Environmental Control and Related Matters

By reason of the nature of many of the Company's operations, environmental standards promulgated by various regulatory bodies, many of which have been recently established, are having or will have a substantial impact upon the Company. In some cases, the Company has obtained variances which are conditioned upon compliance at some future date, and in other cases it is seeking to work out similar arrangements. It is believed that federal and state statutes and regulations dealing with the protection of the environment will increasingly affect the Company. While the exact nature of the environmental control problems which the Company will encounter in the future cannot be predicted, substantial additional capital expenditures and increased operating expenses, the amount of which cannot be estimated at this time, will be occasioned by the Company's continuing effort to deal with environmental problems arising from its activities and to comply with the statutes and regulations referred to above. However, the Company believes that compliance with environmental protection requirements will not adversely affect its competitive position in the industries in which it is engaged. Pollution control requirements resulted in capital expenditures of approximately \$5,800,000 in 1972, \$4,750,000 in 1973, \$7,780,000 in 1974, and \$7,740,000 in 1975. The Company expects to invest an additional amount of approximately \$4,580,000 in pollution abatement facilities in 1976,

\$10,720,000 in 1977, \$3,390,000 in 1978 and \$7,810,000 thereafter. No assurance can be given that the amounts actually invested will not be larger.

On August 30, 1971, the Company entered into an agreement with Rensselaer County Sewer District No. 1 for the construction, operation and maintenance of secondary treatment facilities for the industrial waste discharge from the Company's Rensselaer, N.Y. manufacturing plant. The Company's obligation for the first year of operation, which commenced in June 1976, is presently estimated to be in excess of \$320,000. Of this sum, approximately \$86,000 is estimated to be attributable to debt service. It is anticipated that the operating and maintenance costs for this facility will increase in the future while debt service costs will decrease. The Company's debt service obligation, however, is expected to continue for approximately 27 years. In addition, the Company will be obligated to pay a portion of fixed operating and maintenance costs of the plant through June 30, 1990. Primary treatment for the industrial waste from the Company's plant, as well as the industrial wastes from a plant owned by Sterling Drug Inc. ("Sterling"), is being provided by facilities located adjacent to the Company's plant. Such facilities have been constructed with the proceeds of pollution control revenue bonds (which are unconditionally jointly guaranteed by the Company and Sterling) sold on July 1, 1974 by the Rensselaer County Industrial Development Agency, on which date both the Company and Sterling entered into a ten year lease for such facilities.

On September 26, 1973, and May 24, 1974 pollution control financing arrangements were entered into with, respectively, the City of Calvert City, Kentucky and Broome County Industrial Development Agency (Broome County, New York) pursuant to which pollution control revenue bonds were issued in the respective principal amounts of \$2,700,000 (of which \$300,000 has been prepaid) and \$2,500,000. On June 28, 1975 the Company entered into an additional \$750,000 pollution control financing with Broome County Industrial Development Agency, relating to the project involved in the 1974 financing. All such bonds are unconditionally guaranteed by the Company and the proceeds were used in connection with pollution control facilities at the Company's chemical plant in Calvert City and photo products plant in Binghamton, New York.

On February 20, 1976 the Company entered into an installment sale agreement with the New Jersey Economic Development Authority (the "Authority") for the purchase of pollution control facilities to be constructed by mid-1977 adjacent to the Company's Linden, New Jersey chemical plant with the proceeds of pollution control revenue bonds in the aggregate principal amount of \$10,000,000 sold on that date by the Authority. Payments under the installment sale agreement are assigned to the payment of the Authority bonds, which are also unconditionally guaranteed by the Company. The Company is presently negotiating the use of similar types of financing for pollution control facilities at other locations.

The federal Occupational Safety and Health Administration ("OSHA") has promulgated numerous regulations dealing with various aspects of the Company's operations, including regulation of permissible levels of asbestos fibres in manufacturing facilities. The OSHA regulation applicable to asbestos processing and fabricating facilities established a permissible level in the occupational work atmosphere of five fibres of asbestos per cubic centimeter of air. This permissible level was reduced to two fibres per cubic centimeter on July 1, 1976. The Company's manufacturing operations were in substantial compliance with the five-fibre standard and the Company believes its operations are substantially in compliance with the two-fibre standard. OSHA is presently proposing a further reduction in permissible level to one-half of an asbestos fibre per cubic centimeter of air. The outcome of this proposal and of the effect of any standards which may result therefrom cannot be predicted at

this time. At present the Company is not aware of any adequate substitute for asbestos in the production of roofing felts.

On November 25, 1975, OSHA issued a proposed regulation governing various aspects of industrial use of ammonia. The comment period on these proposals expired in April 1976 and it is expected that OSHA will either issue a revised proposal or call public hearings on the existing proposal in the near future. In addition, OSHA has proposed to terminate the exemption of the diazo industry from an existing regulation governing ammonia use. The Company believes that implementation of either of these proposals would make diazo reproduction operations economically unviable for all but a few of its diazo customers.

The Company is reviewing the recently enacted federal toxic substances control legislation and has preliminarily concluded that such legislation may have a significant effect on the Company's operations. The nature and extent of the impact of this legislation is not ascertainable at this time in light of the fact that regulations have not been proposed.

Facilities

The Company's major plants are as follows:

Chemical: Calvert City, Kentucky; Linden, New Jersey; Rensselaer, New York; Texas City, Texas; Glens Falls, New York; Chattanooga, Tennessee; Glenville, Connecticut; Franklin, Massachusetts; Warren, Michigan; Annapolis, Missouri; Bound Brook, New Jersey; Newburgh, New York; Charmian and Erie, Pennsylvania; and Westerly, Rhode Island. The Company owns rock quarries at Annapolis, Missouri; Charmian, Pennsylvania; and Kremlin, Wisconsin.

Photo & Repro: Binghamton, New York; Philadelphia, Pennsylvania; Los Angeles, California; Sint-Niklaas, Belgium; Progress, Oregon; Vestal, New York; Johnson City, New York; Vernon, New York; Colnbrook, England; Delft, The Netherlands; Shelby, Ohio; Charlotte, North Carolina; San Antonio, Texas; Kansas City, Kansas; Vernon, New York; Arlington, Texas; Milwaukee, Wisconsin; and Sydney, Australia.

Building Materials: Mobile, Alabama; Long Beach, California; Denver Colorado; Tampa, Florida; Savannah, Georgia; Joliet, Illinois; Mount Vernon, Indiana; Baltimore, Maryland; Millis, Massachusetts; Minneapolis, Minnesota; Kansas City and St. Louis, Missouri; Gloucester City and South Bound Brook, New Jersey; Vails Gate, New York; Erie and Whitehall, Pennsylvania; and Dallas and Houston, Texas.

With the exception of the plants located in Warren, Michigan and Annapolis, Missouri, which are leased to the Company, and of two leased buildings in Philadelphia, the above mentioned properties are owned by the Company in fee. That portion of the plant (building and equipment only) at Texas City, Texas which produces AMIBEN® is owned by Amchem.

The Company also owns or leases many other smaller plants, research laboratories, sales offices and distribution warehouses in the United States and elsewhere.

The Company believes that in general these plants and facilities, which are of widely varying ages and of different types of construction, have been adequately maintained and are in good condition. Each plant has adequate transportation facilities for both raw materials and finished products.

The executive offices of the Company and a substantial portion of its administrative offices are housed in approximately 176,000 square feet of leased space at 140 West 51st Street and 1180 Avenue of the Americas, New York, New York.

In July 1972, the Company leased certain laboratory facilities and approximately 100 acres of land in Wayne, New Jersey at which it consolidated a number of its research and development operations. A new 80,000 square foot building, completed in 1974, houses the Company's general administrative and clerical personnel and its principal electronic data processing facilities. The Wayne lease is for a period of 25 years with an option to purchase at expiration. Annual rentals (the lease is a "net lease" under which the Company is obligated to maintain, repair, insure and pay all taxes on the property) are calculated to allow the lessor to recover the cost of the property, its annual interest costs of 7½% and its other expenses of leasing the property. The Company believes that the useful life of most of the buildings remaining at the scheduled termination of the lease will be relatively short.

Litigation and Other Matters

On April 30, 1973 the Company commenced an antitrust action against Eastman Kodak Company. This action is described under the caption "Photo & Repro — Recent Developments."

The Company and Amchem have commenced litigation against one another in several jurisdictions throughout the world. The litigation relates to a plant growth regulator which is sold by Amchem as ETHREL® and by the Company as CERHA®. In several European countries and in the United States Patent Office, the litigation consists of interference proceedings. The interference proceedings brought by the Company in the United States Patent Office were dismissed and in April 1975 a patent relating to certain parts of its application issued to Amchem. In June 1975 the Company commenced a declaratory judgment proceeding in the United States District Court for the Eastern District of Pennsylvania seeking to have the patent granted to Amchem declared invalid and to obtain other appropriate relief. In a separate action brought by the Company in the United States District Court for the Eastern District of Pennsylvania the Court granted Amchem's motion for summary judgment dismissing the Company's suit which sought the assignment to the Company of all Amchem's foreign use patents on the invention of the plant growth regulator and the establishment of a constructive trust in favor of the Company with respect to all of Amchem's profits on ETHREL® sales. The Company is appealing the decision. In another action brought by Amchem in the United States District Court for the Northern District of Georgia, the Court entered judgment dismissing Amchem's suit seeking to cancel the Environmental Protection Agency (the "EPA") registration which the Company had obtained for CERHA®, upon the theory that the Company had obtained such registration pursuant to procedures inconsistent with the Federal Insecticide, Fungicide and Rodenticide Act, as amended. Amchem appealed from this judgment and the United States Court of Appeals for the Fifth Circuit remanded the matter to the district court for the purpose of determining the effect, if any, of recent amendments of that act upon that court's judgment. Upon remand, the district court ruled in the Company's favor, determining that such amendments had no effect upon the outcome. Amchem is appealing this ruling.

In 1974, the Company and eight other United States manufacturers of dyes were indicted on charges of engaging in a combination and conspiracy to fix, raise, and maintain prices of dyes in the United States in violation of Section 1 of the Sherman Act. The government simultaneously brought a civil action, which is still pending, seeking an injunction against the alleged conspiracy and any

other conspiracies or practices of a similar import. Later that year the Company and seven other defendants entered, and the court accepted, pleas of *nolo contendere*. The Company was fined \$45,000 in this action. Shortly after the indictments and civil actions referred to above, six private civil actions were brought against the same defendants by plaintiffs purporting to represent all purchasers of dyestuffs from one or more of these defendants or their alleged co-conspirators. These actions were consolidated in the United States District Court for the Southern District of New York which, in 1975, approved a stipulation of settlement providing for the defendants' to establish a common fund totaling \$15,000,000 for satisfaction of the validated claims of members of the plaintiff class. The Company has made its contribution to this common fund as provided under the approved stipulation of settlement.

During the first quarter of 1976, the Company began an internal investigation of an abuse of one of the Company's cooperative advertising programs during the past several years involving a major domestic customer of the Photo & Repro Group. Under the cooperative advertising program investigated, customers of the Photo & Repro Group were given redeemable scrip equal in face value to a percentage of the amount of their purchases of certain products of that Group. The scrip was redeemable at face value to reimburse customers for approved advertising and, for a time, scrip not used for advertising reimbursement could be used at 25% of face value to order goods from a merchandise catalog. Under the programs now in effect, credits are not redeemable for merchandise and may be used solely for advertising reimbursement. Following a preliminary internal investigation, the Executive Committee of the Board of Directors directed management to cause special outside counsel to conduct a comprehensive investigation of the abuse. That investigation has been completed and special counsel has reported that a senior buyer of that customer, without the knowledge or consent of responsible management of the customer, obtained or directed delivery of between \$150,000 and \$175,000 worth of merchandise during the period 1970 through 1975. Special counsel has also reported that nothing in its investigation revealed any facts which could lead one reasonably to believe that any of the Company's directors or senior management had any information concerning the abuse until it was discovered in December 1975. Management is of the opinion that the abuse of the cooperative advertising program had no material effect upon, and that termination of the merchandise redemption feature of the program has had and will continue to have no material adverse effect upon, the Company's business, financial position or results of operations considered as a whole. The Company has filed Current Reports on Form 8-K with the Securities and Exchange Commission as to the investigation and its results. The Company does not deem the matter to be material.

As of December 1, 1976 the Company was a co-defendant in approximately 210 lawsuits involving alleged health claims of non-employees relating to the inhalation of asbestos fibres. In the only such lawsuit in which judgment after trial was entered against the Company, damages were awarded against a number of co-defendants, including the Company. Such decision was affirmed by the United States Court of Appeals for the Fifth Circuit and certiorari was denied by the United States Supreme Court. The Company has settled certain other of such lawsuits. It is anticipated that additional suits may be filed by industrial insulation workers who have been exposed to asbestos dust at numerous construction sites where insulation materials manufactured by the Company and others were used. The Company has insurance coverage, which is generally subject to a \$50,000 deductible as to each case, with respect to actions of this type. Because premiums paid with regard to such insurance are experience rated, if the Company has an adverse loss experience with respect to such actions, its premiums will be increased to reflect such loss experience. A number of employees and former employees have also filed claims for diseases associated with the inhalation of asbestos fibres under applicable workmen's compensation laws. The Company is self-insured with respect to some of these claims, a

number of which have been settled. The cost to the Company of such settlements and awards in connection with these workmen's compensation claims is not readily ascertainable. The Company does not believe that the disposition of these existing actions and workmen's compensation claims will have a material adverse effect on the Company's earnings or financial position, although the effect on the Company of actions of this nature which may be filed in the future cannot be predicted at this time.

The Company is a defendant (generally one of several) in a number of cases and claims involving allegedly defective roofing. While the amounts claimed in a number of these cases are substantial, the recovery, if any, from the defendants is generally apportioned among them and it is therefore unlikely that the Company would be required to bear the full burden of any judgment or settlement.

DESCRIPTION OF CAPITAL STOCK

The authorized capital stock of the Company consists of 25,000,000 shares of Common Stock, par value \$1.00 per share, and 6,000,000 shares of Preferred Stock, par value \$1.00 per share. On November 30, 1976, 13,769,955 shares of the Company's Common Stock were issued (including 531,599 shares held in treasury) and 3,106,002 shares of a series of the Company's Preferred Stock designated as its \$1.20 Convertible Preferred Stock (the "Convertible Preferred") were issued (including 76,400 shares held in treasury).

All outstanding shares of Common Stock rank equally as to voting rights and dividends and upon liquidation and are fully paid and nonassessable. The Common Stock is not entitled to any preemptive or cumulative voting rights and is not subject to redemption.

Each holder of Convertible Preferred or Common Stock is entitled to one vote for each share held. Except as set forth below, the Convertible Preferred and Common Stock vote together as one class.

The holders of Convertible Preferred are entitled to receive, prior to the payment of dividends on Common Stock, cumulative cash dividends at the rate of \$1.20 per share per year. If dividends are in arrears on the Convertible Preferred in an aggregate amount at least equal to six quarterly dividends, the holders of Convertible Preferred voting as a class will be entitled to elect two directors until all dividends in arrears have been paid and dividends for the current quarterly period have been declared or paid. So long as these dividends are not in arrears, redemption of Convertible Preferred (at \$28 per share through May 31, 1977 and \$27.50 per share thereafter) and the repurchase of either Convertible Preferred or Common Stock are permitted by the Company's Certificate of Incorporation.

The payment by the Company of dividends, other than dividends payable in the Company's capital stock, is subject to restrictions imposed by certain instruments relating to the Company's long-term debt. Under the most restrictive of these provisions approximately \$22,500,000 of the Company's approximately \$323,997,000 retained earnings at October 3, 1976 was available for dividends. The payment of dividends by the Company on its Common Stock is also subject to prior payment of cumulative dividends of \$1.20 per share per year on the Convertible Preferred. Otherwise the Company may pay dividends on its Common Stock out of funds legally available therefor.

Upon any voluntary or involuntary liquidation, dissolution or winding up, before any distribution may be made to the holders of Common Stock, the holders of the Convertible Preferred are entitled to receive \$27.50 per share plus an amount equal to all accrued and unpaid dividends.

Each share of Convertible Preferred is convertible into Common Stock at the rate of 1.25 shares of Common Stock for each share of Convertible Preferred. The conversion rate is subject to adjustment from time to time upon the occurrence of specified events in order to prevent dilution of the appropriate number of shares of Common Stock to be received upon conversion.

Based upon the Company's stock records and upon information furnished to the Company, no person owns of record, or is known by the Company to own beneficially, more than 10% of the Company's outstanding voting securities.

DESCRIPTION OF STOCK PURCHASE PLAN

General

In April 1969 the stockholders of the Company approved the Stock Purchase Plan, under which an aggregate of 650,000 shares of Common Stock was reserved for sale to full-time executive, administrative and supervisory employees of the Company and its participating subsidiaries under 60 years of age. The Plan authorizes the sale of shares subject to prescribed restrictions as to disposition ("Restricted Shares") and without such restrictions ("Unrestricted Shares"). Restricted Shares may not be sold, assigned, transferred, pledged, hypothecated or otherwise disposed of, except as provided in the Plan, for a period of five years from the date of purchase or such further period or periods as may be provided by the Committee of the Board which administers the Plan. If an employee's employment terminates for any reason, other than retirement subsequent to the fifth anniversary of the date of purchase or death subsequent to the completion of five years of continuous employment, the Company has the right to repurchase, at the price which the employee paid for them, the shares which, at the time of termination of employment, remain subject to restrictions. Any shares so repurchased may be resold by the Company. The price of Unrestricted Shares must be at least 80%, and the price of Restricted Shares must be at least 50%, of the closing price of the Company's Common Stock on the New York Stock Exchange on the last trading day on which such stock was traded preceding the date on which an employee is designated as one to whom such shares may be offered for sale. Prior to an amendment of the Plan made in 1973 in connection with the settlement of stockholder litigation concerning the Plan, Restricted Shares could be and were sold at 20% to 40% of such closing price. The purchase of shares under the Plan obligates an employee to remain in the employ of the Company or its subsidiaries for not less than two years in the case of employees who purchase Unrestricted Shares and for not less than three years in the case of employees who purchase Restricted Shares.

All sales under the Plan to date have been of Restricted Shares. No 1978 sales under the Plan have been made as of December 1. Repurchases in 1978, through November 30, from former employees total 5,000 shares.

During 1975 the Company sold for cash an aggregate of 108,000 shares. Of these, 70,000 shares were sold to 12 officers, including 15,000 shares each to Juliette M. Moran and James T. Sherwin, executive vice presidents of the Company, and 38,000 shares to 19 other employees. The sales price was \$5.375 per share; the closing market price on the date of award was \$9.875 per share. A total of 22,000 shares were repurchased in 1975 from former employees.

From the inception of the Plan through the end of 1974 the Company sold an aggregate of 380,000 shares. Of these, 250,000 shares were sold to 29 officers, including 62,000 shares to Dr. Jesse Werner, President and Chairman of the Board, 25,000 shares to Philip B. Dalton, an executive vice president of the Company, 10,000 shares to Miss Merzen and 10,000 shares to Mr. Sherwin,

and 130,000 shares to 59 other employees (of which none subsequently during this period received awards after becoming officers and are also included in such total). The sales prices ranged from \$5,375 to \$5,5625, the closing market prices on the dates of award ranged from \$9.25 to \$29,875. A total of 127,200 shares were repurchased during this period from former employees.

Prior to 1975 certain shares were sold for a minimum of 25% of the purchase price in cash and the balance in six-year promissory notes bearing interest at 6% per year and secured by pledges of all of the shares purchased. As of November 30, 1976, the aggregate outstanding balance of such promissory notes was \$16,125. With respect to the balance of the shares sold during this period, the Company received the entire purchase price in cash at the time of purchase.

As of November 30, 1976, 60 current and retired employees, including officers and directors, held an aggregate of 238,500 shares on which restrictions on sale remain. In addition, as of such date, restrictions on sale had lapsed with respect to 97,000 shares, such restrictions having lapsed on 34,500 shares prior to 1975, on 30,600 shares in 1975 and on 31,600 shares in 1976, through November 30.

As of November 30, 1976 total net proceeds to the Company from the sales under the Plan were \$1,506,737.50.

As of November 30, 1976, there were available for sale to employees under the Plan 316,200 shares. The Company does not presently intend to sell shares under the Plan on a basis other than receipt of the entire purchase price in cash at the time of purchase.

Certain shares sold under the Plan and included in this Prospectus were not registered under the Securities Act of 1933 at the time of issuance since their sale did not involve a public offering, as such term is used in Section 4(2) of such Act.

Tax Effects

The purchase of Restricted Shares under the Plan has no immediate income tax consequences to the Company or an employee, unless an employee makes an election to include an amount in gross income pursuant to Section 83 of the Internal Revenue Code of 1954, as amended (the "Code"). If no such election is made, upon the lapse or removal of the Company's right to repurchase the Restricted Shares at their original purchase price, an employee will recognize ordinary taxable income for Federal income tax purposes in an amount equal to the excess of the fair market value of the shares purchased (determined at the time of such lapse or removal) over the purchase price for such shares, and the Company will be allowed an income tax deduction for compensation expense in the same amount. Upon the subsequent disposition of the shares by an employee he will recognize long-term or short-term capital gain or loss, as the case may be, equal to the difference between the amount realized on such disposition and his basis for the shares, which will generally equal the fair market value of the shares at the time of the lapse or removal of the Company's repurchase right. His holding period for capital gains purposes will commence upon the lapse or removal of the Company's repurchase right.

Section 83 of the Code permits an employee to elect, in the year of purchase of Restricted Shares, to include in his ordinary taxable income the excess of the fair market value of the shares at the time of purchase (determined without regard to any restriction other than a restriction which by its terms will never lapse) over the purchase price for such shares. If such an election is made, the Company will be allowed an income tax deduction for compensation expense in the same amount as is included in the ordinary taxable income of the employee. If, after such election, these shares are subsequently repurchased by the Company pursuant to the Company's right to repurchase at their original purchase price, the employee will not be allowed a deduction with respect to such repurchase. Upon the subse-

quent disposition of Restricted Shares as to which a Section 83 election was made, after the Company's repurchase right lapses or is removed, an employee will recognize long-term or short-term capital gain or loss, as the case may be, equal to the difference between the amount realized on such disposition and his basis for the shares, which will generally equal the fair market value of the shares at the time of purchase. His holding period for capital gains purposes will commence at the time the shares are purchased.

Upon the purchase of Unrestricted Shares under the Plan, an employee will recognize ordinary taxable income for Federal income tax purposes in an amount equal to the excess of the fair market value of the shares purchased (determined at the time of purchase) over the purchase price for such shares, and the Company will be allowed an income tax deduction for compensation expense in the same amount. Upon the subsequent disposition of the shares by an employee he will recognize long-term or short-term capital gain or loss, as the case may be, equal to the difference between the amount realized on such disposition and his basis for the shares, which will generally equal the fair market value of the shares at the time of purchase. His holding period for capital gains purposes will commence at the time the shares are purchased.

The ordinary taxable income realized by an employee upon the lapse or removal of restrictions on the disposition of Restricted Shares, upon the making of an election pursuant to Section 83 of the Code, or upon the purchase of Unrestricted Shares under the Plan will (i) if realized in a taxable year beginning before January 1, 1977, be eligible, under proposed Treasury regulations, for the 50% maximum rate of tax on "earned taxable income", and (ii) if realized in a taxable year beginning after December 31, 1976, be eligible, under the Tax Reform Act of 1976, for the 50% maximum rate of tax on "personal service income".

The above discussion of certain relevant Federal income tax provisions is a summary only and reference is made to the Internal Revenue Code of 1954, as amended, and the applicable regulations thereunder for a complete statement of all relevant Federal tax provisions. It is recommended that employees consult their tax advisers before purchase or disposition of any shares.

FINANCIAL STATEMENTS — EXPERT'S

The financial statements of the Company included in this Prospectus, excluding the Nine Months (Unaudited) Consolidated Financial Statements, have been examined by Haskins & Sells, independent certified public accountants, as stated in their opinion appearing herein and have been so included in reliance upon such opinion given upon their authority as experts in accounting and auditing.

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OPINION OF INDEPENDENT CERTIFIED PUBLIC ACCOUNTANTS

GAF CORPORATION:

We have examined the consolidated balance sheet of GAF Corporation and its consolidated subsidiaries as of December 31, 1975 and 1974, and the related consolidated statements of income, stockholders' equity and changes in financial position for the five years ended December 31, 1975. Our examination was made in accordance with generally accepted auditing standards, and accordingly included such tests of the accounting records and such other auditing procedures as we considered necessary in the circumstances.

In our opinion, such financial statements present fairly the financial position of the companies at December 31, 1975 and 1974 and the results of their operations and the changes in their financial position for the five years ended December 31, 1975, in conformity with generally accepted accounting principles which have been applied on a consistent basis after restatement for the change, with which we concur, in the method of accounting for foreign currency translation described in Note B and except for the changes, with which we concur, in methods of accounting for certain inventories and of determining income before extraordinary items as described in Notes C and H to the Consolidated Statement of Income, and for the change made as of January 1, 1971, with which we concur, in the method of accounting for the investment tax credit as described in Note I to the Consolidated Financial Statements.

HASKINS & SELLS

New York, New York
February 6, 1976

CAF CORPORATION AND CONSOLIDATED SUBSIDIARIES

CONSOLIDATED BALANCE SHEET

ASSETS

	December 31,	
	1975	1974
	(Note B)	
	Dollars in Thousands	
CURRENT ASSETS		
Cash	\$ 8,448	\$ 15,072
Marketable securities, at cost which approximates quoted market value	4,175	163
Accounts receivable — trade, less allowance for doubtful accounts — 1975, \$4,908,000; 1974, \$3,902,000	151,233	153,965
Accounts receivable — other	10,159	7,983
Inventories (Notes 1 and C)		
Finished goods	106,180	105,647
Work in process	46,329	43,948
Raw materials and supplies	78,432	99,865
Total inventories	230,941	249,480
Prepaid expenses	6,523	8,537
Total current assets	411,479	435,180
PROPERTY, PLANT AND EQUIPMENT AT COST (Notes 1 and 4)		
Land and land improvements	15,083	14,724
Buildings and building equipment	104,585	100,867
Machinery and equipment	270,839	255,048
Construction in progress	17,076	21,143
Total property, plant and equipment	407,583	391,782
Less accumulated depreciation	163,815	160,140
Property, plant and equipment — net	243,768	231,642
OTHER ASSETS		
Cost in excess of net assets acquired (Note 1)	34,790	34,998
Other investments and advances (Notes 3 and A)	8,153	2,297
Other assets	7,443	5,332
Total other assets	50,386	42,627
TOTAL ASSETS	\$705,433	\$709,449

See Notes to Consolidated Financial Statements.

Alphabetic note references are to the Notes to Consolidated Statement of Income included elsewhere in this Prospectus.

GAF CORPORATION AND CONSOLIDATED SUBSIDIARIES

CONSOLIDATED BALANCE SHEET

LIABILITIES

	December 31,	
	1975	1974 (Note B)
	Dollars in Thousands	
CURRENT LIABILITIES		
Notes payable (Note 6)		
Banks	\$ 11,374	\$ 13,368
Commercial paper	—	6,240
Other	10,380	12,823
Current portion of long-term debt (Note 6)	27,683	5,243
Accounts payable		
Trade	42,829	39,225
Other	4,187	3,091
Accrued liabilities		
Payroll	3,171	3,708
Retirement plan	9,879	6,801
Other taxes	5,412	4,078
Interest	1,772	1,845
Other	20,893	24,021
United States and foreign income taxes	6,071	10,444
Total current liabilities	143,651	130,887
LONG-TERM DEBT LESS CURRENT PORTION (Note 6)	139,168	181,173
DEFERRED CREDITS		
Deferred income taxes (Notes 1, 5 and J)	35,231	31,884
Deferred investment tax credit (Note 1)	3,726	4,298
Total deferred credits	38,957	36,182
OTHER LIABILITIES	4,626	3,619
COMMITMENTS AND CONTINGENT LIABILITIES (Note 12)		
STOCKHOLDERS' EQUITY		
Preferred Stock, \$1 par value; authorized 6,000,000 shares; \$1.20 convertible series; issued — 1975, 3,105,706 shares; 1974, 3,105,411 shares; at assigned value of \$1.25 per share (liquidation value 1975, \$83,306,000) (Note 7)	3,882	3,882
Common Stock, \$1 par value; authorized 25,000,000 shares; issued — 1975, 13,764,090 shares; 1974, 13,763,715 shares (Note 7)	13,764	13,764
Additional paid-in capital	53,151	52,791
Retained earnings	313,546	293,108
Total	384,343	363,545
Less stock held in treasury, at cost:		
Common — 1975, 534,949 shares; 1974, 620,949 shares	4,380	5,025
Preferred — 1975, 76,400 shares; 1974, 76,400 shares	932	932
Total stockholders' equity (Note 6)	379,031	357,588
TOTAL LIABILITIES AND STOCKHOLDERS' EQUITY	\$705,433	\$709,449

See Notes to Consolidated Financial Statements.

Alphabetic note references are to the Notes to Consolidated Statement of Income included elsewhere in this Prospectus.

GAF CORPORATION AND CONSOLIDATED SUBSIDIARIES
CONSOLIDATED STATEMENT OF CHANGES IN FINANCIAL POSITION

	Year Ended December 31,				
	1975	1974 (Note B)	1973 (Note B)	1972	1971
	Dollars in Thousands				
Funds Provided					
From operations:					
Income before extraordinary items	\$ 30,946	\$ 28,517	\$ 31,819	\$ 27,706	\$ 21,907
Charges (credits) not affecting working capital:					
Depreciation	25,026	24,212	23,200	25,400	24,550
Deferred income taxes (noncurrent portion)	3,347	1,351	1,769	2,847	2,462
Gain on reacquisition of 5% convertible notes	—	(5,523)	(6,359)	—	—
Office relocation expenses (noncurrent portion) (Note G)	369	1,858	—	—	—
Translation losses (gains) (noncurrent portion)	640	4,255	(1,150)	—	—
Phase-out of Linden dyestuff manufacturing (Note H)	—	—	5,942	—	—
Other	459	92	590	(382)	(62)
Funds provided from operations exclusive of extraordinary items	<u>60,787</u>	<u>54,762</u>	<u>55,811</u>	<u>55,571</u>	<u>48,857</u>
Extraordinary items	—	—	—	—	(8,433)
Charges (credits) included in extraordinary items not affecting working capital:					
Net book value of facilities sold	—	—	—	—	23,301
Deferred income taxes (noncurrent portion)	—	—	—	—	(3,313)
Unamortized deferred investment tax credit	—	—	—	—	(804)
Funds provided from extraordinary items	<u>—</u>	<u>—</u>	<u>—</u>	<u>—</u>	<u>10,751</u>
Funds provided from operations	<u>60,787</u>	<u>54,762</u>	<u>55,811</u>	<u>55,571</u>	<u>59,608</u>
Issuance of long-term debt	1,072	65,980	57,530	—	15,000
Property, plant and equipment dispositions	803	4,643	2,395	2,321	1,100
Proceeds from exercise of stock options and sale of restricted stock to key employees	580	27	672	1,039	641
Other	(2,030)	580	210	(824)	(2,557)
Total	\$ 61,212	\$125,972	\$116,618	\$ 58,107	\$ 73,792

(Consolidated Statement of Changes in Financial Position is continued on the following page)

GAF CORPORATION AND CONSOLIDATED SUBSIDIARIES
CONSOLIDATED STATEMENT OF CHANGES IN FINANCIAL POSITION — (Continued)

	Year Ended December 31,				
	1975	1974 (Note B)	1973 (Note B)	1972	1971
	Dollars in Thousands				
Funds Applied					
Additions to property, plant and equipment	\$ 37,995	\$ 39,288	\$ 25,933	\$ 29,022	\$ 29,939
Cash dividends	10,508	9,923	9,452	9,231	9,246
Reacquisition of \$18,500,000 and \$23,200,000 principal amount of 5% convertible notes less related gains of \$5,523,000 and \$6,359,000 in 1974 and 1973, respectively	—	12,977	16,841	—	—
Other reductions in long-term debt	42,505	6,278	18,780	16,161	18,121
Investment in joint venture company (Note A)	6,549	—	—	—	—
Acquisitions of common stock for treasury	120	3,718	2,434	668	54
Acquisition of preferred stock for treasury	—	932	—	—	—
Net assets, excluding working capital, of businesses purchased	—	—	—	—	16,513
Total	97,677	73,116	73,440	55,082	73,873
Increase (Decrease) in Working Capital (including \$545,000 in 1971 arising from purchases of businesses)	(36,465)	52,856	43,178	3,025	(81)
Working Capital, January 1	304,293	251,437	208,259	205,234	205,315
Working Capital, December 31	\$267,828	\$304,293	\$251,437	\$208,259	\$205,234

ANALYSIS OF CHANGES IN WORKING CAPITAL

Increase (decrease) in current assets:					
Cash and marketable securities	\$ (2,612)	\$ 1,185	\$ (5,769)	\$ 2,691	\$ 3,131
Accounts receivable — trade	(2,732)	3,202	14,034	11,919	12,775
Accounts receivable — other	2,176	1,074	1,658	(5,708)	1,784
Inventories	(18,519)	66,592	11,358	15,106	9,498
Prepaid expenses	(2,014)	(839)	2,372	(2,695)	2,028
	<u>(23,701)</u>	<u>71,214</u>	<u>23,653</u>	<u>21,313</u>	<u>29,216</u>
Increase (decrease) in current liabilities:					
Notes payable	(10,677)	4,997	(13,808)	20,469	6,105
Current portion of long-term debt	22,440	4,350	(14,495)	(2,819)	5,790
Accounts payable	4,700	(1,533)	4,844	5,167	2,195
Accrued liabilities	674	8,228	4,340	1,183	7,741
United States and foreign income taxes	(4,373)	2,316	(406)	(5,712)	7,468
	<u>12,784</u>	<u>18,358</u>	<u>(19,525)</u>	<u>18,288</u>	<u>29,297</u>
Increase (decrease) in working capital	\$ (36,465)	\$ 52,856	\$ 43,178	\$ 3,025	\$ (81)

See Notes to Consolidated Financial Statements.

Alphabetic note references are to the Notes to Consolidated Statement of Income included elsewhere in this Prospectus.

GAF CORPORATION AND CONSOLIDATED SUBSIDIARIES

CONSOLIDATED STATEMENT OF STOCKHOLDERS' EQUITY

For the Five Years Ended December 31, 1975

	Preferred Stock		Common Stock \$1 Par Value		Retained Earnings	Treasury Stock		
	Number of Shares Issued	Assigned Value	Number of Shares Issued	Additional Paid In Capital		Pre- ferred	Com- mon	Cost
Balance, January 1, 1971	3,163,071	\$3,954,000	13,598,828	\$50,058,000	\$229,444,000	—	5,000	\$ 27,000
Net income					13,474,000			
Cash dividends:								
Preferred stock — \$1.20 per share					(3,802,000)			
Common stock — \$.40 per share					(5,444,000)			
Stock options exercised	7,840	9,000	3,700	172,000				
Issuance of shares under an incentive compensation plan assumed by the Company	243			5,000				
Issuance of restricted shares of common stock under Stock Purchase Plan			14,000	61,000				
Conversion of preferred stock	(1,050)	(1,000)	1,312					
Purchase of treasury shares							10,000	54,000
Sale of treasury shares							(5,000)	(27,000)
Amortization of excess of quoted market value over ag- gregate sales price of re- stricted shares sold under the Stock Purchase Plan (Note 8)				254,000				
Balance, December 31, 1971	3,170,104	\$3,962,000	13,617,840	\$50,550,000	\$233,672,000	—	10,000	\$ 54,000
Net income					27,706,000			
Cash dividends:								
Preferred stock — \$1.20 per share					(3,759,000)			
Common stock — \$.40 per share					(5,472,000)			
Stock options exercised	2,815	4,000	57,750	977,000				
Issuance of shares under an incentive compensation plan assumed by the Company	582	1,000		13,000				
Conversion of preferred stock	(69,393)	(87,000)	86,738					
Purchase of treasury shares							43,500	668,000
Issuance of treasury shares in connection with an acqui- sition							(17,291)	(427,000)
Amortization of excess of quoted market value over ag- gregate sales price of re- stricted shares sold under the Stock Purchase Plan (Note 8)				180,000				
Other				49,000				
Balance, December 31, 1972	3,104,108	\$3,880,000	13,762,328	\$51,769,000	\$252,147,000	—	36,209	\$ 295,000

(Consolidated Statement of Stockholders' Equity is continued on the following page)

GAF CORPORATION AND CONSOLIDATED SUBSIDIARIES

CONSOLIDATED STATEMENT OF STOCKHOLDERS' EQUITY — (Continued)

For the Five Years Ended December 31, 1975

	Preferred Stock		Common Stock \$1 Par Value	Additional Paid In Capital	Retained Earnings	Treasury Stock		
	Number of Shares Issued	Assigned Value	Number of Shares Issued			Pre- ferred	Com- mon	Cost
Balance, December 31, 1972 ..	3,104,108	\$3,880,000	13,762,328	\$51,769,000	\$252,147,000	—	36,209	\$ 295,000
Net income (Note B)					31,819,000			
Cash dividends:								
Preferred stock — \$1.20 per share					(3,726,000)			
Common stock — \$.42 per share					(5,726,000)			
Stock options exercised			1,000	9,000				
Issuance of shares under an incentive compensation plan assumed by the Company ..	981	1,000		21,000				
Conversion of preferred stock ..	(80)		100					
Purchase of treasury shares ..							173,000	2,434,000
Issuance of treasury shares in connection with sales under the Stock Purchase Plan ..				(732,000)			(119,000)	(1,394,000)
Issuance of treasury shares in connection with a prior ac- quisition				1,000			(60)	(1,000)
Amortization of excess of quoted market value over ag- gregate sales price of re- stricted shares sold under the Stock Purchase Plan (Note 8)				985,000				
Balance, December 31, 1973 ..	3,105,009	\$3,881,000	13,763,428	\$52,053,000	\$274,514,000	—	90,149	\$1,334,000
Net income (Note B)					28,517,000			
Cash dividends:								
Preferred stock — \$1.20 per share					(3,705,000)			
Common stock — \$.46 per share					(6,218,000)			
Issuance of shares under an incentive compensation plan assumed by the Company ..	632	1,000		14,000				
Conversion of preferred stock ..	(230)		287					
Purchase of treasury shares:								
Preferred stock						76,400		832,000
Common stock							535,800	3,718,000
Issuance of treasury shares in connection with sales under the Stock Purchase Plan ..				(1,000)			(5,000)	(27,000)
Amortization of excess of quoted market value over ag- gregate sales price of re- stricted shares sold under the Stock Purchase Plan (Note 8)				725,000				
Balance, December 31, 1974 ..	3,105,411	\$3,882,000	13,763,715	\$52,791,000	\$293,108,000	76,400	620,949	\$5,957,000

(Consolidated Statement of Stockholders' Equity is continued on the following page)

GAF CORPORATION AND CONSOLIDATED SUBSIDIARIES

CONSOLIDATED STATEMENT OF STOCKHOLDERS' EQUITY — (Continued)

For the Five Years Ended December 31, 1975

	Preferred Stock		Common Stock \$1 Par Value		Retained Earnings	Treasury Stock		
	Number of Shares Issued	Assigned Value	Number of Shares Issued	Additional Paid In Capital		Number of Shares		Cost
Balance, December 31, 1974	3,105,411	\$3,882,000	13,763,715	\$52,791,000	\$293,108,000	76,400	620,949	\$5,957,000
Net income					30,940,000			
Cash dividends:								
Preferred Stock — \$1.20 per share					(3,635,000)			
Common Stock — \$.52 per share					(6,873,000)			
Issuance of shares under an incentive compensation plan assumed by the Company	595	1,000		13,000				
Conversion of preferred stock	(300)	(1,000)	375					
Purchase of treasury shares							22,000	120,000
Issuance of treasury shares in connection with sales under the Stock Purchase Plan				(185,000)			(108,000)	(765,000)
Amortization of excess of quoted market value over ag- gregate sales price of re- stricted shares sold under the Stock Purchase Plan (Note 8)								
Balance, December 31, 1975	<u>3,105,706</u>	<u>\$3,882,000</u>	<u>13,764,090</u>	<u>\$53,151,000</u>	<u>\$313,548,000</u>	<u>76,400</u>	<u>534,949</u>	<u>\$5,312,000</u>

See Notes to Consolidated Financial Statements.

Alphabetic note references are to the Notes to Consolidated
Statement of Income included elsewhere in this Prospectus.

GAF CORPORATION AND CONSOLIDATED SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

(Alphabetic note references are to Notes to the Consolidated Statement of Income included elsewhere in this Prospectus.)

Note 1. Summary of Significant Accounting Policies

The accounts of all significant subsidiaries of the Company are included in the consolidated financial statements.

Translation of Foreign Currencies — Cash, accounts receivables and liabilities of foreign subsidiaries are translated into U.S. dollars at current exchange rates; all other assets, deferred income taxes and depreciation are translated at historical rates. Operating accounts, except for depreciation, are translated using average exchange rates to approximate the rates in effect when transactions were consummated.

Foreign exchange gains and losses are included in net income for the period in which the exchange rate changes.

Inventories — Inventories, other than dyestuffs and pigments, are valued at the lower of cost (principally average) or market. Effective with the year ended December 31, 1974, dyestuffs and pigments inventories are valued at cost, determined by the last-in, first-out (LIFO) method.

Property, Plant and Equipment, and Related Depreciation — Expenditures for maintenance and repairs are charged directly to expense; major replacements and betterments are capitalized and depreciated over the remaining estimated economic lives of the related assets. The cost and related accumulated depreciation of property sold, retired or fully depreciated are removed from the accounts and any resultant gain or loss is included in current income.

Depreciation is computed principally on the straight-line method based on the estimated economic lives of the assets. These lives are subject to annual review and revision to assure that the cost of the related assets is written off over their economic lives.

Cost in Excess of Net Assets Acquired — Cost in excess of net assets acquired in connection with acquisitions prior to November 1, 1970 is not being amortized because there has been no diminution in value; such cost relating to acquisitions made subsequent to October 31, 1970, all of which has continuing value, is being amortized on the straight-line method over a period of forty years.

Deferred Income Taxes — Deferred income taxes arise from reporting certain income and expense items in the financial statements in periods different from those in which such amounts are reported for United States income tax purposes.

Investment Tax Credit — The Company accounts for investment tax credits arising since January 1, 1971 as a reduction of the provision for United States income tax (the flow-through method). Investment tax credits which arose prior to that date have been deferred and are being amortized over the estimated service lives of the related assets.

Research and Development Costs — Expenditures for research and development are charged to income as incurred.

CAF CORPORATION AND CONSOLIDATED SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS — (Continued)

Note 1. Summary of Significant Accounting Policies — (Continued)

Retirement Plans — The Company and its subsidiaries have several retirement plans covering substantially all employees. The Company's policy is to fund amounts equal to pension costs accrued and, for plans with prior service costs, to amortize such costs over periods not to exceed forty years.

Earnings per Share — Primary earnings per common share are computed by dividing net income, less preferred stock dividend requirements, by the weighted average number of shares of common stock outstanding during the year. The computation assumes the exercise of outstanding stock options to the extent they are dilutive.

Fully diluted earnings per common share are computed on the assumption (where the effect thereof would be dilutive) that convertible securities outstanding had been converted into shares of common stock. Appropriate adjustments for dividends on preferred stock and interest on convertible notes (net of income tax effect) are made to earnings applicable to common stock for assumed conversions. The computation also assumes the exercise of all dilutive stock options.

Note 2. Foreign Operations

The consolidated balance sheet includes the following amounts with respect to foreign subsidiaries (all of which are wholly-owned):

	December 31,	
	1975	1974*
	Dollars in Thousands	
Current assets	\$72,814	\$74,727
Other assets	12,691	10,689
Total assets	85,505	85,616
Current liabilities	28,137	35,498
Other liabilities	8,645	5,928
Total liabilities	36,782	41,426
Net assets	\$48,723	\$44,190

The consolidated statement of income includes the following amounts with respect to foreign subsidiaries:

	Year ended December 31,				
	1975	1974*	1973*	1972	1971
	Dollars in Thousands				
Net sales	\$135,526	\$129,172	\$106,414	\$78,849	\$84,364
Income before extraordinary items	\$ 5,248	\$ 5,201	\$ 8,196	\$ 2,576	\$ 3,128
Extraordinary credits	—	—	—	—	1,153
Net income	\$ 5,248	\$ 5,201	\$ 8,196	\$ 2,576	\$ 4,279

* Restated — See Note B to Consolidated Statement of Income.

GAF CORPORATION AND CONSOLIDATED SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS — (Continued)

Note 3. Acquisitions

In March 1971, the Company acquired certain photofinishing plants and the business and assets relating thereto for a net cash purchase price of approximately \$15,200,000. The results of operations of the acquired business, which did not significantly affect consolidated revenues or net income for 1971, have been included in the consolidated financial statements from the date of acquisition.

In 1972, the Company completed studies (including independent appraisals) to determine the fair value of certain assets included in the 1971 acquisition and recorded at that time at tentative values. As a result of these studies certain reallocations, which did not have a significant effect on the consolidated financial statements, of these tentative values were made.

The Company's ownership of an Australian subsidiary, GAF (Australasia) Pty. Limited (formerly Consolidated Reprographics, Ltd.), was increased to 100% at December 31, 1972 through cash purchases of this subsidiary's shares of capital stock from minority stockholders amounting to approximately \$156,000 in 1972 and \$1,479,000 in 1971.

Note 4. Property, Plant and Equipment

The ranges of annual depreciation rates generally were as follows:

Land improvements	2 %-10%
Buildings and building equipment	1½%-10%
Machinery and equipment	3 %-40%

Note 5. Income Taxes

Provision has not been made for the United States income taxes on unremitted earnings of foreign subsidiaries of \$34,987,000, since any withholding taxes and United States income taxes payable on dividends based on undistributed earnings would be substantially offset by foreign tax credits or because the remittance of such earnings has been indefinitely postponed. United States income taxes have not been provided on the unremitted earnings of the Domestic International Sales Corporation subsidiary aggregating \$7,758,000 through December 31, 1975, since the Company intends to postpone indefinitely the remittance of such earnings.

The principal sources of United States deferred taxes are:

	1975	1974
	Dollars in Thousands	
Excess of tax depreciation over amount reported in Consolidated Statement of Income	\$2,614	\$2,297
Gain on reacquisition of 5% convertible notes	—	2,714
Foreign exchange transactions (Note B)	(730)	(2,497)
Office relocation expenses	87	(1,352)
Other — net	952	(1,917)
	<u>\$2,923</u>	<u>\$ (755)</u>

CAF CORPORATION AND CONSOLIDATED SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS — (Continued)

Note 5. Income Taxes — (Continued)

The effective tax rates were 33.5% and 42.4% in 1975 and 1974, respectively. The reasons for the differences from the statutory rate of 48.0% are as follows:

	% of Pretax Income	
	1975	1974
Statutory rate	48.0 %	48.0 %
Increases (decreases) in taxes resulting from:		
Gain on sale of technology and know-how	(8.6)	—
United States investment tax credit	(7.5)	(4.1)
State and local income taxes, net of United States income tax benefit	2.2	2.3
Domestic International Sales Corporation — DISC	(2.9)	(1.8)
Other — net	2.3	(2.0)
Effective tax rate	<u>33.5 %</u>	<u>42.4 %</u>

Note 6. Debt and Dividend Restrictions

Long-term debt at December 31, 1975 and 1974 was as follows:

	1975	1974
	Dollars in Thousands	
6½% Swiss Franc Note due October 1, 1976	\$ 19,085	\$ 19,650
Promissory Notes, payable to banks, due May 15, 1980	24,000	24,000
Promissory Notes payable to banks, due December 31, 1981	48,000	60,000
5½% Convertible Subordinated Notes due April 1, 1983 with annual repayments of \$200,000 on each April 1 through 1982 and the balance of \$1,800,000 payable April 1, 1983	3,200	3,400
5% Convertible Subordinated Notes due April 1, 1994 with annual repayments beginning April 1, 1990	8,200	8,200
5½% Sinking Fund Debentures due December 1, 1991 with annual sinking fund payments of \$2,500,000 on each December 1, less \$2,869,000 and \$1,653,000 in treasury in 1975 and 1974, respectively	37,131	40,847
Other notes, which bear interest at 3% to 9% and mature at various dates to 1986	<u>27,235</u>	<u>30,319</u>
Total	166,851	186,416
Less portion due within one year	<u>27,683</u>	<u>5,243</u>
Long-term debt, less current portion	<u>\$139,168</u>	<u>\$181,173</u>

The promissory notes due in 1980 bear interest at 122% of the prime commercial lending rate through May 15, 1978 and 128% of such rate thereafter. Outstanding borrowings at December 31, 1975 are repayable in quarterly installments commencing in 1976.

GAF CORPORATION AND CONSOLIDATED SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS — (Continued)

Note 6. Debt and Dividend Restrictions — (Continued)

The promissory notes due in 1981 bear interest at 115% of the prime commercial lending rate. Outstanding borrowings at December 31, 1976 are repayable in quarterly installments commencing in 1978. Pursuant to arrangements in connection with these notes, a compensating balance of 10% (\$4,800,000 at December 31, 1975) of the outstanding debt is to be maintained.

The 5½% convertible subordinated notes are convertible into shares of common stock, at any time prior to April 2, 1976, at a conversion price of \$28.72 per share (subject to anti-dilution adjustments in specified circumstances).

The 5% convertible subordinated notes are convertible into shares of common stock, at any time, at a conversion price of \$27.50 per share (subject to anti-dilution adjustments in specified circumstances).

The total amount of long-term debt maturing in 1977 is \$10,179,000, in 1978, \$23,389,000, in 1979, \$23,399,000, and in 1980, \$19,178,000. The 5½% Sinking Fund Debenture, held in treasury may be used to reduce the amount of the annual sinking fund payments. None of the long-term debt is pledged, held by or for the account of the Company, or held in sinking or other special funds, except for \$2,869,000 and \$1,653,000 of the 5½% Sinking Fund Debentures held in treasury at December 31, 1975 and December 31, 1974, respectively.

At December 31, 1975, the Company had domestic lines of credit aggregating \$52,500,000 with interest generally at the prime commercial lending rate. Pursuant to certain of the domestic arrangements under which lines of credit were established, compensating balances are generally required to equal 20% of the outstanding borrowings and 10% of the unused portion of the lines of credit. At December 31, 1975, there were no borrowings in connection with the lines of credit and compensating balances amounted to approximately \$4,250,000.

Dividends are restricted under provisions of certain loan agreements. Under the most restrictive of these provisions, stockholders' equity cannot be reduced below \$348,214,000. Stockholders' equity at December 31, 1975 was \$379,031,000.

Short-term debt at December 31, 1975 was \$21,754,000 as compared with an average of \$36,177,000 for the year 1975; the maximum amount of such borrowings outstanding at any month-end during 1975 was \$53,808,000. The average interest rate on the year-end balance was 8.0% as compared with an average of 8.3% for the full year.

Note 7. Capital Stock

The \$1.20 convertible preferred stock, dividends on which are cumulative, is convertible at any time into common stock at the rate (subject to anti-dilution adjustments in certain circumstances) of 1½ shares of common stock for each share of preferred. The Company may redeem the preferred stock at specified prices ranging from \$28.50 per share through May 31, 1976 to \$27.50 per share after May 31, 1977 (subject to anti-dilution adjustments in specified circumstances).

GAF CORPORATION AND CONSOLIDATED SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS — (Continued)

Note 7. Capital Stock — (Continued)

The voluntary or involuntary liquidation value of the 3,029,306 outstanding shares (3,105,706 shares issued less 76,400 shares held in treasury) of \$1.20 convertible preferred stock at December 31, 1975, aggregating \$83,306,000, exceeds the assigned value by \$26.25 per share, or a total of \$79,519,000. In the opinion of counsel for the Company, retained earnings are not restricted as to payment of dividends on common stock by reason of the liquidation preferences of the \$1.20 convertible preferred stock.

The number of shares of the Company's capital stock reserved for issuance at December 31, 1975 and 1974 were as follows:

	1975	1974
\$1.20 Convertible Preferred Stock:		
Reserved for payment of deferred stock awards under an incentive compensation plan assumed by the Company	921	1,516
Common Stock:		
Reserved for conversion of \$1.20 Convertible Preferred Stock, including 1,151 and 1,895 shares, respectively, for deferred stock awards	3,737,784	3,788,159
Reserved for exercise of stock options	1,112,500	509,750
Reserved for conversion of 5½% Convertible Subordinated Notes	111,420	118,384
Reserved for conversion of 5% Convertible Subordinated Notes	298,182	298,182
Reserved for sale under the Stock Purchase Plan	311,200	397,200
Total	5,621,086	5,111,675

None of the shares outstanding is held by or for the account of the issuer thereof and no shares, other than stated above, are reserved for officers and employees or for options, warrants, conversions, or other rights.

Note 8. Stock Option and Stock Purchase Plans

The 1975 Stock Option Plan (the "1975 Plan") authorizes the grant of qualified and non-qualified stock options for 800,000 shares to key employees during a ten-year period ending February 11, 1985. The prices at which options may be granted may not be less than 100% of the fair market value of the shares on the dates the options are granted.

Subsequent to approval of the 1975 Plan by the holders of approximately 80% of the stock voting at the 1975 Annual Meeting of Stockholders (approximately 48.5% of the outstanding shares of voting stock), the Internal Revenue Service issued a ruling with retroactive application requiring approval by more than 50% of the outstanding voting stock for the 1975 Plan to be treated as a "qualified" plan. Accordingly, the 1975 Plan is being resubmitted to stockholders at the 1976 Annual Meeting for approval as a qualified and non-qualified stock option plan in accordance with the requirements of the Internal Revenue Service and for approval as a non-qualified plan only. No options have been granted under the 1975 Plan, and none will be granted unless the 1975 Plan is approved by the stockholders at the 1976 Annual Meeting.

The Company's 1965 Qualified Stock Option Plan (the "1965 Plan") expired on March 31, 1975. Under the provisions of the 1965 Plan, options to purchase shares of common stock were granted to key employees during a ten-year period. No further options may be granted under the 1965 Plan. The

GAF CORPORATION AND CONSOLIDATED SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS — (Continued)

Note 8. Stock Option and Stock Purchase Plans — (Continued)

prices at which options were granted were not less than 100% of the fair market value of the shares on the dates the options were granted. The options are exercisable after a one-year waiting period and terminate five years from date of grant.

Options outstanding by year of grant at December 31, 1975 and 1974 were as follows:

Year of Grant	Option Price Per Share	1975		1974	
		Number of Shares	Total Option Price	Number of Shares	Total Option Price
1970	\$10.1875-11.000	—	\$ —	8,300	\$ 86,000
1972	20.875	37,500	783,000	41,500	866,000
1973	12.687	68,500	869,000	74,250	942,000
1974	9.500	46,000	437,000	54,000	513,000
1975	9.69	160,500	1,555,000	—	—
		<u>312,500</u>	<u>\$3,644,000</u>	<u>178,050</u>	<u>\$2,407,000</u>

At December 31, 1975 and 1974 there were 800,000 and 331,700 shares, respectively, of common stock reserved for the granting of additional options.

Common Stock options became exercisable as follows:

Year Exercisable	Number of Shares	Option Price		Market Price on Date First Exercisable	
		Per Share	Total	Per Share	Total
1971	31,000	\$10.1875-11.000	\$ 319,000	\$19.687-19.937	\$ 611,000
1972	—	—	—	—	—
1973	68,000	20.875-23.375	1,445,000	10.937-11.562	750,000
1974	74,250	12.687	942,000	8.687	645,000
1975	54,000	9.50	513,000	10.125	547,000

Common stock options exercised were as follows:

Year Ended December 31,	Number of Shares	Option Price		Market Price on Date Exercised	
		Per Share	Total	Per Share	Total
1971	3,700	\$10.1875-17.313	\$ 45,000	\$19.75-24.625	\$ 80,000
1972	57,750	10.1875-25.375	997,000	21.125-27.00	1,434,000
1973	1,000	10.1875	10,000	14.812-21.1875	15,000
1974	—	—	—	—	—
1975	—	—	—	—	—

Options for 152,000 and 124,050 shares of common stock, having an aggregate option price of \$2,089,000 and \$1,894,000, respectively, were exercisable at December 31, 1975 and 1974, respectively.

GAF CORPORATION AND CONSOLIDATED SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS — (Continued)

Note 8. Stock Option and Stock Purchase Plans — (Continued)

\$1.20 Convertible Preferred Stock options exercised were as follows:

Year Ended December 31,	Number of Shares	Option Price		Market Price on Date Exercised	
		Per Share	Total	Per Share	Total
1971	7,840	\$13.500-18.375	\$ 140,000	\$21.000-30.750	\$ 178,000
1972	2,815	13.500-17.750	42,000	28.125-32.000	86,000
1973	—	—	—	—	—
1974	—	—	—	—	—
1975	—	—	—	—	—

The proceeds from stock options exercised were credited to the preferred and common stock accounts in the amount of the assigned or par values of the respective shares issued, and the excess was credited to additional paid-in capital.

Under the provisions of the Company's 1969 restricted and unrestricted stock purchase plan, 650,000 shares of common stock may be sold to key employees. The stock purchase plan as originally adopted provided that restricted and unrestricted shares may be sold at prices which are not less than 20% and 80%, respectively, of the closing market price preceding the date on which an employee is designated as one to whom shares may be offered for sale. The minimum purchase price of restricted shares under the stock purchase plan was raised from 20% to 50% of such market price in accordance with a court-approved settlement terminating certain stockholders' derivative litigation. The excess of quoted market value over the aggregate sales price for restricted shares sold is being amortized by charges to income over the restriction period. The unamortized balance to be amortized through 1984 amounted to \$1,150,000 and \$1,316,000 at December 31, 1975 and 1974, respectively. Under certain conditions, the Company has the right to repurchase restricted shares of common stock at the original selling price. These repurchased shares are held in treasury.

Note 9. Retirement Plans

The following is a summary of pension costs:

<u>Year</u>	<u>Amount</u>
1975	\$11,797,000
1974	9,282,000
1973	6,777,000
1972	5,981,000
1971	5,539,000

CAF CORPORATION AND CONSOLIDATED SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS — (Continued)

Note 9. Retirement Plans — (Continued)

The actuarially computed value of vested benefits exceeded the total of pension funds and accrued liabilities for pension costs by \$53,200,000 at December 31, 1975. The estimated unfunded prior service cost at December 31, 1975 was \$58,800,000. The Company does not anticipate any significant increase in the required contributions to the pension funds as a result of the 1974 pension reform act. However, under the act, the Company is liable in the event of termination of plans for any guaranteed benefits (as defined by the act) in excess of the plans' net assets, limited to 30% of the Company's net worth at the time of termination. Such liability for guaranteed benefits at December 31, 1975 is not readily determinable, but would be less than the unfunded vested benefits at that date. Following the general increase in security prices during 1975, the market value of the funds increased substantially.

Note 10. Executive Incentive Compensation

The Company has an Executive Incentive Compensation Plan that provides for bonuses to key executives of the Company based on consolidated net income (as defined). The provision for such bonuses was as follows:

Year	Amount
1975	\$1,599,000
1974	2,273,000
1973	1,754,000
1972	1,624,000
1971	1,285,000

Note 11. Supplementary Income Statement Information

The following table summarizes supplementary income statement information for the five years ended December 31, 1975.

	Charged to Costs and Expenses For the Year Ended December 31,				
	1975	1974	1973	1972	1971
	Dollars in Thousands				
Maintenance and repairs	\$41,704	\$41,344	\$36,079	\$34,059	\$33,823
Depreciation of property, plant and equipment	25,026	24,212	23,200	25,400	24,550
Taxes, other than taxes on income:					
Social Security and unemployment	10,550	15,388	14,521	12,475	9,385
Other	7,977	7,738	7,430	7,173	6,650
Rent	14,607	14,532	14,062	13,263	12,022

GAF CORPORATION AND CONSOLIDATED SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS — (Continued)

Note 11. Supplementary Income Statement Information — (Continued)

Approximately 40% of rent expense is applicable to noncapitalized financing leases (as defined by the Securities and Exchange Commission). If the assets associated with such leases had been capitalized, the effect on net income would not have been significant in either 1975 or 1974. However, in such event, the expense presently recorded as rent would be comprised of two different elements (i.e. amortization of leaseholds and imputed interest). The amortization would represent the major portion of this expense.

Note 12. Commitments and Contingent Liabilities

The Company is obligated under various long-term, noncancelable leases at December 31, 1975 as follows:

	Land and Land Improvements	Minimum Rental by Period		Total
		Buildings and Building Equipment	Machinery and Equipment	
		Dollars in Thousands		
1976	\$ 36	\$ 4,534	\$ 4,569	\$ 9,139
1977	32	4,287	1,964	6,283
1978	32	3,911	1,312	5,255
1979	37	3,575	665	4,277
1980	37	3,358	344	3,737
1981-1985	183	10,589	407	17,179
1986-1990	154	11,115	196	11,465
1991-1995	5	8,275	—	8,280
Beyond 1995	10	3,389	—	3,399

The above amounts are for existing leases and do not represent a forecast of future expenses.

Approximately 60% of all rental commitments are applicable to noncapitalized financing leases. The present value of commitments applicable to these leases is less than five percent of the sum of long-term debt, stockholders' equity and the present value of such leases.

The Company had commitments of approximately \$12,585,000 at December 31, 1975 for the acquisition of property, plant and equipment.

At December 31, 1975, there were certain lawsuits and claims pending against the Company. In the opinion of management, the ultimate disposition of these matters will not materially affect the Company's consolidated financial position.